No. 15-

IN THE

Supreme Court of the United States

APPLE INC.,

Petitioner,

v.

UNITED STATES OF AMERICA, *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

In 2010 Apple launched the revolutionary iPad, and with it, the iBookstore, an innovative retail platform; together, they disrupted Amazon's dominant position in the e-books market. Apple entered with a new agency business model, concluding vertical arrangements with e-book publishers that included commonplace provisions that are often procompetitive and unquestionably served Apple's legitimate business objectives in offering consumers a new e-books platform. Yet a divided court of appeals panel condemned Apple's conduct as *per se* unlawful under Section 1 of the Sherman Act because its vertical activities supposedly facilitated horizontal collusion among the publishers, who wished to be free from Amazon's dominance. The panel majority declined to follow this Court's decision in *Leegin Creative Leather Products, Inc.* v. *PSKS, Inc.*, 551 U.S. 877 (2007), which instructed that such vertical conduct must be analyzed under the rule of reason, and also rejected another circuit's decision that properly followed *Leegin*.

The question presented is:

> Whether vertical conduct by a disruptive market entrant, aimed at securing suppliers for a new retail platform, should be condemned as *per se* illegal under Section 1 of the Sherman Act, rather than analyzed under the rule of reason, because such vertical activity also had the alleged effect of facilitating horizontal collusion among the suppliers.

PARTIES TO THE PROCEEDING

Petitioner is Apple Inc., a defendant-appellant in the court of appeals.

Respondents, and plaintiffs-appellees in the court of appeals, are the United States of America; the State of Texas; the State of Connecticut; the Commonwealth of Puerto Rico; the State of Utah; the State of Alabama; the State of Alaska; the State of South Dakota; the State of North Dakota; the District of Columbia; the State of Indiana; the State of Arizona; the State of Tennessee; the State of Nebraska; the State of Michigan; the State of Colorado; the State of Vermont; the Commonwealth of Massachusetts; the State of Illinois; the State of West Virginia; the State of New Mexico; the State of Iowa; the Commonwealth of Virginia; the State of Kansas; the State of Maryland; the State of New York; the State of Idaho; the State of Missouri; the State of Arkansas; the State of Ohio; the State of Louisiana; the Commonwealth of Pennsylvania; the State of Wisconsin; and the State of Delaware.

Defendants-appellants in the court of appeals, who are not petitioners here, are Simon & Schuster, Inc.; Simon & Schuster Digital Sales, Inc.; Verlagsgruppe Georg Von Holtzbrinck GmbH; and Holtzbrinck Publishers, LLC, DBA Macmillan. Defendants in the district court, who are not petitioners here, are Hachette Book Group, Inc.; HarperCollins Publishers L.L.C.; and The Penguin Group, a Division of Pearson PLC, Penguin Group (USA), Inc.

CORPORATE DISCLOSURE STATEMENT

Petitioner Apple Inc. has no parent corporation. To the best of Apple's knowledge and belief, and based on public filings with the Securities and Exchange Commission, as of October 26, 2015, no publicly held corporation owns 10% or more of Apple's stock.

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PETITION FOR A WRIT OF CERTIORARI

Apple Inc. respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit in this case.

INTRODUCTION

Apple's launch of the iBookstore as a platform for tens of millions of consumers to buy and read digital books ("e-books") on the iPad dramatically enhanced competition in the e-books market, benefitting authors, e-book publishers, and retail consumers. Following Apple's entry, output increased, overall prices decreased, and a major new retailer began to compete in a market formerly dominated by a single firm. As the district court acknowledged: "[H]aving the creativity and commitment of Apple invested in the enhancement of a product like the iBookstore [was] extremely beneficial to consumers and competition." App. 248a n.69. Yet a divided panel of the Second Circuit deemed the procompetitive nature of Apple's entry irrelevant and held Apple's conduct *per se* unlawful because, in entering the e-books market through its vertical dealings with five e-book publishers, Apple was found also to have facilitated horizontal collusion among the publishers.

The panel majority's decision contradicts this Court's precedent and, as Judge Jacobs explained in dissent, "creates a circuit split, and puts [the Second Circuit] on the wrong side of it." App. 106a. Under Section 1 of the Sherman Act, 15 U.S.C. § 1, the presumptive standard for evaluating whether a defendant's conduct unreasonably restrains trade is the rule of reason. *Leegin Creative Leather Prods., Inc.* v. *PSKS, Inc.*, 551 U.S. 877, 885 (2007). Unlike the *per se* rule, the rule of reason requires assessment of the real-world competitive effects of the challenged conduct. *Id.* Condemnation under the *per se* rule is "appropriate only" for conduct that "'would always or almost always tend to restrict competition'" and "only after courts have had considerable experience with the type of restraint at issue." *Id.* at 886. Moreover, *per se* condemnation is not appropriate for genuine "vertical" arrangements between firms at different levels of the industry structure, such as Apple (an e-book retailer) and the publishers (e-book suppliers), as opposed to "horizontal" arrangements between competitors. That is because vertical conduct often brings procompetitive effects. *Id.* at 889-894.

The panel majority sought to justify its result by characterizing Apple's vertical conduct in assembling a new content platform as "orchestrat[ing]" *per se* illegal horizontal collusion among e-book publishers. App. 55a. The panel's ruling is contrary to this Court's precedent and creates a conflict with the Third Circuit. *Toledo Mack Sales & Serv., Inc.* v. *Mack Trucks, Inc.*, 530 F.3d 204 (3d Cir. 2008) (reviewing a vertical agreement that allegedly facilitated a horizontal conspiracy under the rule of reason). And the panel majority's error is even more clear because, as the government conceded, "no court ha[d] previously considered a restraint" like Apple's agreements with publishers, App. 108a (Jacobs, J. dissenting), and, as the panel majority acknowledged, the "nascent" e-books market had "new and unusual features," App. 69a.

The Second Circuit's decision will harm competition and the national economy. It threatens to subject procompetitive vertical conduct to categorical antitrust condemnation, contrary to this Court's repeated recognition that vertical conduct often enhances competition and its repeated decisions "to temper, limit, or overrule once strict prohibitions on vertical restraints," *Leegin*, 551 U.S. at 901. And the Second Circuit's approach creates intolerable uncertainty over how courts will assess vertical conduct accused of having horizontal effects—uncertainty that will chill innovation and risk-taking.

This Court should grant the petition, confirm that vertical activity, undertaken for bona fide, potentially procompetitive purposes, is not transformed into *per se* illegal conduct merely because it also has been found to facilitate horizontal collusion, and overturn the court of appeals' erroneous application of the *per se* rule.

OPINIONS BELOW

The opinion of the court of appeals (App. 1a-119a) is reported at 791 F.3d 290. The decision of the district court (App. 121a-250a) is reported at 952 F. Supp. 2d 638.

JURISDICTION

The judgment of the court of appeals was entered on June 30, 2015. App. 1a. On September 17, 2015, Justice Ginsburg extended the time for filing a petition for certiorari to October 28, 2015. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

Section 1 of the Sherman Act, 15 U.S.C. § 1, provides in relevant part:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal.

STATEMENT

Apple, a newcomer to the world of digital books, succeeded in delivering an innovative retail platform to consumers that disrupted the incumbent's dominant position. The question in this case is whether Apple may nevertheless be subjected to *per se* antitrust liability because the courts below found that its vertical dealings with suppliers (book publishers) made it easier for the publishers to engage in alleged horizontal collusion among themselves.

A. The E-Books Market Before Apple's Entry

Before Apple entered the e-books market, that market was dominated by a single firm: Amazon. App. 95a. Amazon used a "loss leader" strategy, under which it sold new releases and best-seller e-books at $9.99—less than the wholesale prices Amazon paid e-book publishers—to attract sales for Amazon's other products. App. 2a, 8a-9a.

Because any new entrant "'would run the risk of losing money if it tried'" to match Amazon's below-cost pricing, Amazon's strategy deterred new competitors from innovating and offering readers new e-book platforms. App. 95a (quoting 149a). By 2009, Amazon claimed almost 90% of the e-books retail market and faced virtually no competition. App. 96a & n.2, 130a.

With no real alternative retail platform for e-books—and thus no other outlet to reach readers—publishers were forced to accept Amazon's terms for selling e-books to consumers, including the loss-leading retail model, which publishers believed undermined their interests. App. 95a-96a. Among other things, publishers believed that Amazon's strategy cannibalized hardcover book sales, threatened the viability of brick-and-mortar bookstores that generate demand for titles, and devalued books in the eyes of consumers. App. 95a, 131a. Given Amazon's dominance, however, the publishers had little recourse. One of the publishers' few potential options was to withhold e-books from Amazon for a period of time, a practice known as "windowing." App. 135a-137a & n.10. But windowing came with serious costs; it made books unavailable to consumers in digital form, alienated e-book readers, encouraged piracy, and harmed long-term book sales. App. 139a.

B. Apple Develops The iBookstore And Enters The Market

In late 2009, Apple was preparing to launch the iPad, a "revolutionary" tablet with "remarkable features" that made an e-book reader "an obvious addition to the device." App. 247a-248a & n.69. Apple sought to develop the iBookstore, a competing platform for purchasing e-books that could be read on the iPad. App. 142a-145a.

The iBookstore is an example of a content platform, which has emerged as a common element of digital commerce. Content platforms benefit consumers by aggregating content from diverse suppliers into convenient, feature-rich forums that are easy for consumers to use. Shelanski, *Information, Innovation, and Competition Policy for the Internet*, 161 U. Pa. L. Rev. 1663, 1666-1666 (2013). For the iBookstore, publishers were the relevant content suppliers and Apple was the assembler.

In that role, with the iPad launch scheduled for January 2010, Apple opened negotiations with each of the six largest publishers in December 2009.[1] App. 13a-14a. The press had already reported that the publishers were eager for a new e-book platform to provide an alternative to Amazon. App. 14a, 135a-138a, 144a. In separate meetings, Apple told the publishers that it was negotiating with each of them and that it wanted to begin selling e-books within 90 days. App. 14a-15a.[2]

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[1] In 2009, there were six major e-book publishers. Five—Hachette, HarperCollins, Macmillan, Penguin, and Simon & Schuster—were defendants in this action; the largest publisher (Random House) was not.

[2] According to the courts below, the publishers had long been coordinating to move Amazon from its loss-leader model before

Apple also discussed with its potential suppliers their own requirements and preferences. *Id.*

To create a viable content platform and enter the market as an e-book retailer, Apple needed to attract a critical mass of publishers so that it could provide a broad, compelling e-book selection to consumers. App. 14a-15a, 231a. It also needed a business model that would allow it to offer competitive prices while also making a profit. App. 16a-17a, 97a-98a. Apple was not prepared to adopt a loss-leader strategy, to offer e-books at prices that were not competitive with Amazon's, or to offer consumers less than a rich and current selection. App. 15a, 215a, 231a.

Over the course of extensive negotiations, Apple developed a vertical business model that would enable it to meet those goals and thus to enter the e-books market. App. 149a-155a. Its vertical contracting structure had three core components. First, it used an "agency," rather than wholesale, model: Instead of buying e-books from publishers and reselling them, Apple would act as each publisher's agent, selling the publisher's e-books at the iBookstore at a retail price set by that publisher, with Apple taking a commission on each sale. App. 97a-98a. Second, the vertical agreements had "most-favored-nation" ("MFN") clauses requiring each publisher to price its iBookstore offerings no higher than the price offered by any other e-book retailer. App. 98a. Third, the vertical agreements capped the maximum price each publisher could set for various categories of e-books sold at the iBookstore. *Id.*

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their respective negotiations with Apple began. *E.g.*, App. 9a-12a. This petition does not depend on any challenge to that finding.

Those interrelated provisions advanced Apple's independent business interests and facilitated its entry into the e-books market. The agency model allowed Apple to offer competitive retail prices to consumers while also turning a profit; by contrast, under a wholesale model, Apple would have risked being unable to negotiate e-book wholesale prices low enough to profitably offer e-books at competitive prices. App. 16a-17a, 114a-115a. The MFN clause ensured that iBookstore titles would be sold at prices that were competitive with other e-book retailers, allowing Apple to be price competitive with Amazon for best-sellers and other popular titles, which Amazon was selling below its own costs. App. 157a. Finally, the price caps ensured that a publisher would not set its iBookstore prices so high as to damage the iBookstore's or Apple's credibility with consumers. As the district court found, these contracting terms and Apple's negotiation tactics are commonplace and certainly not inherently illegal. App. 228a.

In attempting to assemble a critical mass for its iBookstore, Apple faced another reality as well: It had to convince enough publishers that its business model was sufficiently attractive for them to join. Apple offered the above terms to each publisher in separate emails sent on January 11, 2010. App. 19a-20a. After additional negotiations—including "intense" negotiations over the price caps, App. 166a-173a—Apple proposed revised terms to each publisher several days later and renewed its efforts to persuade each publisher to sell through the iBookstore. App. 22a-23a.[3] Consistent

[3] The negotiations were hard-fought because the parties' interests on this point were at odds; Apple wanted lower price caps to avoid "alienat[ing]" consumers, whereas the publishers would have preferred no caps at all. App. 172a.

with its goal of maximizing publisher participation in its new platform, Apple reminded the publishers that its entry, using the agency model, represented their best hope of challenging Amazon's dominance and gaining an effective alternative to Amazon's below-cost pricing, which undermined the publishers' business strategy. *E.g.*, App. 23a-24a, 44a-45a, 49a. And Apple again told each publisher that it could not launch the iBookstore without a sufficient number of e-book suppliers. App. 23a, 48a-49a. In that regard, during its final push, Apple kept the publishers "'apprised about who was in and how many were on board,'" assuring each publisher that the iBookstore would be successful and that they would not be alone if Amazon retaliated against them for joining, as the publishers feared it would. App. 23a-26a, 49a, 132a, 216a-217a.

Apple ultimately succeeded in negotiating terms that would allow it to enter the e-books market. When the iPad launched on January 27, 2010, five of the six largest publishers had signed on to the iBookstore. App. 27a.

Apple's entry and the emergence of its new e-books platform introduced substantial innovation and competition into the e-books sector and disrupted Amazon's dominance, both as a buyer from publishers and as a retailer to consumers. Amazon's share of e-book retailing was reduced from almost 90% to 60%, and output of e-books sharply increased. App. 66a-67a, 99a, 112a-113a. Expert testimony established that overall e-book prices declined following Apple's entry. App. 67a, 201a-202a, 220a n.61. The iPad was a "revolutionary" product in e-reading hardware and software as well as in digital publishing. App. 112a-113a, 231a, 247a-248a. Tens of millions of consumers now purchase and read e-books on the iPad, using the iBookstore platform. And

Apple's entry, and the agency structure, replaced Amazon's dominance with a multitude of price setters. App. 111a-112a.[4]

Development of Apple's new e-books platform also meant that publishers were no longer at the mercy of Amazon as an e-book distributor and had new leverage to negotiate with it. App. 188a-189a. Immediately after Apple announced the iBookstore, the publishers that had signed vertical agreements with Apple began negotiating new terms with Amazon. By June 2010, Amazon had agreed to an agency model with each of them. App. 30a.[5]

C. Proceedings Below

In April 2012, the United States and 33 States (together "the government") sued Apple and the five publishers that joined the iBookstore at its launch, alleging that Apple and the publishers had violated Section 1 of the Sherman Act, 15 U.S.C. § 1. The government principally asserted that the publishers had engaged in a horizontal price-fixing conspiracy to raise e-book retail prices by moving Amazon away from a wholesale model, and that Apple had committed a *per se* violation by entering *vertical* agency agreements with the publishers that supposedly "facilitated" the publishers' alleged *horizontal* conspiracy. Compl. ¶¶ 6-7, 97. The government

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[4] There was no allegation, and no evidence, that the publishers agreed not to compete with each other once they had obtained the ability to set prices.

[5] The courts below found that, during negotiations between Amazon and the publishers, the publishers communicated with one another in an effort to present a united front and force concessions. App. 99a, 196a. Again, this petition does not depend on challenging that finding.

also asserted that the defendants' conduct violated Section 1 under a rule-of-reason analysis. Compl. ¶ 98.

The publishers ultimately entered into consent decrees with the government but did not admit liability. Apple—believing it had done nothing wrong and that its entrance into the e-books market was procompetitive—proceeded to trial. App. 34a-36a. At trial, the government conceded that neither the terms of Apple's contracts with the publishers nor its negotiating tactics were themselves unlawful. App. 228a. And the district court expressly declined to find that Apple desired to increase e-book prices, the object of the publishers' supposed horizontal conspiracy. App. 244a n.68. But the district court nonetheless agreed with the government that Apple should be condemned under the categorical *per se* rule because its vertical conduct facilitated an agreement among the publishers to join forces against Amazon. In a one-paragraph analysis, the district court also found Apple liable under the rule of reason, App. 219a-220a, even though it also acknowledged that Apple was acting in its "independent, economic interests" and seeking "to create a profitable iBookstore on a superior e-reader," and that Apple's goal of launching the iBookstore was "admirable" and "extremely beneficial to consumers and competition," App. 227a, 231a, 232a, 248a n.69.

A fractured panel of the Second Circuit affirmed based solely on application of the *per se* rule, App. 6a, 90a, in a decision that produced three separate opinions. In an opinion by Judge Livingston, a panel majority concluded that Apple committed a *per se* violation by "orchestrat[ing]" a horizontal conspiracy among the publishers to raise e-book prices. App. 55a. The majority reasoned that the *per se* rule's application depended on "the type of restraint" imposed, irrespective of whether Apple's own conduct was vertical or horizontal in nature. App. 55a-58a. The majority conceded that Apple's vertical conduct "might well, if challenged, have to be evaluated under the rule of reason," App. 57a, but nonetheless ruled that the relevant "'agreement in restraint of trade'" was the publishers' horizontal conspiracy, App. 57a, 61a.

The panel majority acknowledged this Court's statement in *Leegin* that "if a 'vertical agreement setting minimum resale prices is entered upon to facilitate' a horizontal cartel, it 'would need to be held unlawful under the rule of reason.'" App. 59a-60a (quoting *Leegin Creative Leather Products, Inc.* v. *PSKS, Inc.*, 551 U.S. 877, 893 (2007)). It declined to follow that statement, however, dismissing it as a "cryptic sentence" that did not foreclose *per se* condemnation in this case. App. 60a. The panel majority considered *Leegin* inapposite because it did not address a scenario where the defendant "'participated in an unlawful horizontal cartel with [its] *competing retailers*,'" App. 59a (quoting *Leegin*, 551 U.S. at 907-908) (emphasis and bracketed text added)—even though there was no allegation in this case that Apple conspired with its own e-book retailer rivals. The panel majority also believed *Leegin* did not extend to so-called "hub-and-spoke" cases, where "the vertical organizer … has also agreed to participate in the horizontal conspiracy." App. 60a-61a.

Judge Livingston, writing for herself only, alternatively would have affirmed based on a "quick look" rule-of-reason analysis. App. 69a-82a. Judge Lohier, however, joined only the portion of Judge Livingston's opinion discussing the *per se* rule and declined to join the portion relating to the rule of reason, concluding that "Apple's appeal rises or falls based on the application of the per se rule." App. 90a.

Judge Jacobs dissented. He read this Court's decision in *Leegin* and other authority as directing that Apple's vertical conduct be evaluated under the rule of reason. App. 101a-104a. Judge Jacobs observed that the majority's application of the *per se* rule "creates a circuit split" with *Toledo Mack Sales & Service, Inc.* v. *Mack Trucks, Inc.*, 530 F.3d 204 (3d Cir. 2008), "and puts us on the wrong side of it." App. 104a-106a. Judge Jacobs would have reversed the district court based on a full rule-of-reason analysis because "Apple's conduct … was unambiguously and overwhelmingly procompetitive." App. 94a; *see also* App. 109a-116a. "Apple took steps to compete with a monopolist and open the market to more entrants, generating only minor competitive restraints in the process. Its conduct was eminently reasonable; no one has suggested a viable alternative." App. 116a.

REASONS FOR GRANTING THE PETITION

I. THE DECISION OF THE COURT OF APPEALS CONFLICTS WITH DECISIONS OF THIS COURT AND CREATES A CIRCUIT SPLIT

The Second Circuit's application of the *per se* rule to Apple's novel, vertical conduct conflicts with *Leegin Creative Leather Products, Inc.* v. *PSKS, Inc.*, 551 U.S. 877 (2007), and other decisions of this Court, and creates an acknowledged division in the circuits. Only by erroneously dismissing a key point in *Leegin* as a nonbinding "cryptic sentence," App. 60a, was the panel majority able to apply the *per se* rule here. The panel's flawed ruling threatens to forestall procompetitive conduct—the exact result this Court's modern antitrust decisions have sought to avoid.

A. Application Of The *Per Se* Rule To Apple's Vertical Conduct Conflicts With This Court's Decision In *Leegin* And Creates A Circuit Split

Section 1 of the Sherman Act "'outlaw[s] only unreasonable restraints'" of trade. *Leegin*, 551 U.S. at 885 (quoting *State Oil Co.* v. *Khan*, 522 U.S. 3, 10 (1997)). Accordingly, "the accepted standard for testing whether a practice restrains trade in violation of § 1" is the "rule of reason," which requires a court to consider "'all of the circumstances of a case'" in order to "distinguish[] between restraints with anticompetitive effect that are harmful to the consumer and restraints stimulating competition that are in the consumer's best interest." *Id.* at 885, 886. Only a narrow set of horizontal agreements (*i.e.*, agreements among competitors) may be "'deemed unlawful *per se*,'" without any inquiry into their reasonableness "in light of real world market forces." *Id.* at 886.[6]

This Court has repeatedly made clear, most recently in *Leegin*, that genuine vertical activities—like a retailer's business arrangements with suppliers—are assessed under the rule of reason, not the *per se* rule. The Court's modern cases have consistently "rejected the approach of reliance on rules governing horizontal restraints when defining rules applicable to vertical ones." *Leegin*, 551 U.S. at 888. Accordingly, over the last four decades, this Court has "continued to temper,

[6] *Per* se unlawful conduct "include[s] horizontal agreements among competitors to fix prices, or to divide markets," *Leegin*, 551 U.S. at 886 (citation omitted), and certain forms of group boycott agreements, *e.g.*, *Klor's, Inc.* v. *Broadway-Hale Stores, Inc.*, 359 U.S. 207, 212 (1959). Apple was not accused of entering into any agreement with a competitor or participating in any group boycott.

limit, or overrule once strict prohibitions on vertical restraints." *Id.* at 901 (overruling precedent and holding that vertical resale price maintenance is subject to the rule of reason); *Khan*, 522 U.S. at 21-22 (overruling precedent and holding that vertical maximum price maintenance agreements are subject to the rule of reason); *Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36, 57-59 (1977) (overruling precedent and holding that vertical non-price restraints are subject to the rule of reason).

This Court has rejected *per se* treatment for vertical conduct because vertical conduct often has "procompetitive effects." *Leegin*, 551 U.S. at 901. The "differences in economic effect between vertical and horizontal agreements" mean that a real-world analysis of market effects from vertical conduct—*i.e.*, analysis under the rule of reason—is always required to avoid subjecting potentially procompetitive activity to categorical liability. *Id.* at 888; *see also Khan*, 522 U.S. at 11, 14-17 (discussing how "vertical maximum price fixing … is not necessarily harmful to competition and consumers" and can have procompetitive benefits); *Sylvania*, 433 U.S. at 50-51, 54 (discussing the "redeeming virtues" of vertical restrictions).

"[A]ll vertical restraints … have the potential" to facilitate unlawful collusion among horizontal competitors. *Business Elecs. Corp.* v. *Sharp Elecs. Corp.*, 485 U.S. 717, 728 (1988). Where, as here, vertical conduct is accused of having had that effect, the conduct is no less subject to assessment under rule of reason. In *Leegin*, this Court recognized that resale price maintenance has the potential to "facilitate" a *per se* illegal horizontal cartel at the manufacturer or retailer level. 551 U.S. at 892-893. Nonetheless, the Court stated that "[t]o the extent a vertical agreement setting minimum resale prices is entered upon to facilitate either type of cartel, it … would need to be held unlawful *under the rule of reason*." *Id.* at 893 (emphasis added); *see also Khan*, 522 U.S. at 17 (even if vertical maximum price-fixing agreement were "used to disguise" unlawful conduct, such conduct still "can be appropriately recognized and punished under the rule of reason").

Here, the Second Circuit departed from *Leegin* by incorrectly applying the *per se* rule to Apple's vertical dealings with e-book publishers, bypassing any assessment of the real-world competitive effects of Apple's entry into the e-books market. The panel majority deemed Apple's vertical dealings with publishers *per se* unlawful because those dealings supposedly "facilitated" *horizontal* "price-fixing" by the publishers. App. 36a, 61a. Not only did that reasoning ignore this Court's repeated mandate that *per se* treatment is inappropriate for legitimate vertical activity because it so often brings procompetitive benefits, *e.g.*, *Leegin*, 551 U.S. at 888, it also disregarded the broader context of Apple's entry and enhancement of competition in the e-books market.

Apple's conduct was vertical in nature—as a prospective e-books retailer, it was negotiating with its prospective suppliers regarding the terms of supply. *See Business Elecs.*, 485 U.S. at 730. Both the panel majority and the district court recognized that agency agreements, MFN clauses, and price caps—all of which indisputably flowed from these supplier negotiations—are not in themselves unlawful and can be entirely appropriate business strategies. App. 57a, 228a. No aspect of Apple's vertical activity—either the terms of the agreements themselves or Apple's efforts to persuade suppliers to participate in the iBookstore platform—was found to be a sham designed solely to promote a publisher horizontal conspiracy or otherwise not genuinely related to Apple's efforts to enter the market in a sustainable way.

Under *Leegin*, Apple's bona fide vertical conduct cannot be condemned as illegal *per se*, and the procompetitive benefits of that conduct cannot be ignored, even if it supposedly "facilitate[d] [a publisher] cartel." 551 U.S. at 893. In ruling otherwise, the panel majority elided *Leegin*'s express, on-point direction as a "cryptic sentence," App. 60a, and wrongly labeled Apple's vertical conduct as an "agree[ment] to participate in the horizontal conspiracy," App. 61a. This Court should correct the panel majority's error.

Moreover, as Judge Jacobs recognized, "[t]he majority's holding … creates a circuit split, and puts [the Second Circuit] on the wrong side of it." App. 106a. In *Toledo Mack Sales & Service, Inc.* v. *Mack Trucks, Inc.*, 530 F.3d 204, 225 (3d Cir. 2008), the Third Circuit properly followed *Leegin* to hold that "[t]he rule of reason analysis applies even when … the plaintiff alleges that the purpose of the vertical agreement between a manufacturer and its dealers is to support illegal horizontal agreements between multiple dealers." Toledo, a former truck dealer, asserted a two-part conspiracy, involving both horizontal collusion among dealers not to compete on price and a vertical agreement between the dealers and manufacturer Mack, under which Mack agreed to punish dealers that cheated on the arrangement. *Id.* at 209-210. Although the horizontal agreement in *Toledo Mack* was deemed *per se* unlawful, the Third Circuit, relying on *Leegin*, correctly held that the rule of reason applied to the vertical agreement between Mack and its dealers. *Id.* at 225 & n.15 (citing *Leegin*, 551 U.S. at 893, and abrogating pre-*Leegin* circuit authority);[7] *see also, e.g.*, *In re Musical Instruments & Equip. Antitrust Litig.*, 798 F.3d 1186, 1192-1193 (9th Cir. 2015) (distinguishing vertical and horizontal components of an alleged conspiracy).

The Second Circuit's decision cannot be reconciled with *Toledo Mack*. Had this case arisen in the Third Circuit, Apple's conduct would have been assessed under the rule of reason, consistent with *Leegin*. Indeed, Apple's accused vertical arrangements present an even stronger case for the rule of reason than *Toledo Mack*. In that case, the only purpose of the challenged vertical conduct was to facilitate horizontal collusion, 530 F.3d at 225, whereas here the courts below acknowledged Apple's "independent business reasons for creating an e-bookstore," and its "entirely appropriate or even admirable motives." *E.g.*, App. 230a-231a. Yet the panel majority still condemned Apple's conduct as illegal *per se*. The conflict is clear and ripe, and requires resolution.

B. Application Of The *Per Se* Rule To The Novel Circumstances Of This Case Also Conflicts With This Court's Precedents

The court of appeals' decision also conflicts with this Court's admonition that *per se* treatment is appropriate only for restraints that history and judicial experience have shown lack any redeeming value and are unquestionably anticompetitive, such that they would

[7] The Third Circuit has since confirmed its holding. *In re Insurance Brokerage Antitrust Litig.*, 618 F.3d 300, 318-319 (3d Cir. 2010). The panel majority's statement that "[t]he panel in *Insurance Brokerage* … had no occasion to revisit *Toledo Mack*," App. 61a n.20, is both incomplete and irrelevant. *Insurance Brokerage* expressly distinguished vertical agreements from related horizontal ones and applied the rule of reason to the former, 618 F.3d at 318-319—exactly what the panel majority failed to do here.

fail the rule of reason "in … almost all instances." *Leegin*, 551 U.S. at 886-887; *see also Khan*, 522 U.S. at 10. As the Seventh Circuit has explained, "[i]t is a bad idea to subject a novel way of doing business (or an old way in a new and previously unexamined context) … to per se treatment …. The per se rule is designed for cases in which experience has convinced the judiciary that a particular type of business practice has no … redeeming benefits ever." *In re Sulfuric Acid Antitrust Litig.*, 703 F.3d 1004, 1011-1012 (7th Cir. 2012). Repeated experience is required before courts can be sure that their "departure from the rule-of-reason standard [is] based upon demonstrable economic effect rather than … formalistic line drawing." *Sylvania*, 433 U.S. at 58-59.

The circumstances here plainly raise issues new to the federal courts. Using a combination of vertical arrangements that the government conceded "no court ha[d] previously considered," App. 108a, Apple pursued entry into a "nascent" digital market that had been dominated from inception by a single firm, App. 3a, 69a. Its conduct brought many market effects that the district court acknowledged were "extremely beneficial to consumers and competition," App. 248a n.69, including an innovative retail platform for consumers, new content and increased e-book output, and the disruption of Amazon's dominance as both a wholesale purchaser and retailer of e-books. No court had *ever* considered the constellation of contract terms at issue here, let alone conclusively determined their effects on competition in *this* market, which the panel majority acknowledged was "new and at least arguably involves some new ways of doing business." App. 54a; *see also* Shelanski, 161 U. Pa. L. Rev. at 1685 ("The characteristics of digital platforms make competition enforcement more challenging than usual.").

Given that the courts have never addressed the unique combination of business arrangements present here or the resulting complex economic analysis that is required, this is decidedly not an appropriate case in which to forgo inquiry into real-world competitive effects. *E.g.*, *Broadcast Music, Inc.* v. *Columbia Broad. Sys., Inc.*, 441 U.S. 1, 10 (1979) (rejecting *per se* rule for conduct that had been labeled as "price fixing" by court below and observing that "[w]e have never examined a practice like this one before"); *Sulfuric Acid*, 703 F.3d at 1012 (rejecting *per se* rule in novel circumstances involving market entry); *see also*, *e.g.*, *Sylvania*, 433 U.S. at 53-54 n.22 (noting the potential for "additional exceptions to the *per se* rule for new entrants in an industry"). As Judge Jacobs explained, "the analysis [of Apple's conduct] is sufficiently complex and yields such substantial pro-competitive results that *per se* liability is an abdication of the duty to distinguish reasonable restraints from those that are unreasonable." App. 108a. This Court should correct the panel majority's erroneous application of the *per se* rule to the highly novel circumstances of this case.[8]

C. The Second Circuit's Reasons For Applying The *Per Se* Rule Are Flawed And Inconsistent With This Court's Antitrust Jurisprudence

The panel majority's reasons for treating Apple's vertical conduct as *per se* illegal were conceptually

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[8] Applying "quick look" rule-of-reason analysis, as suggested by Judge Livingston writing only for herself, App. 70a, would have been error as well. Quick-look analysis is appropriate only where "an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets." *California Dental Ass'n* v. *FTC*, 526 U.S. 756, 770 (1999); *see also id.* at 777-778.

flawed in at least two ways: The majority conflated vertical and horizontal conduct, and it misinterpreted the "hub-and-spoke" cases.

1. The panel majority disregarded the crucial distinction between Apple's vertical conduct and the publishers' alleged horizontal conspiracy, because Apple supposedly understood that the agency agreements it was offering would create incentives for the publishers collectively to move Amazon to an agency model and used negotiating strategies directed at convincing the publishers to join its new iBookstore. App. 44a-50a. In the panel majority's view, even though none of Apple's conduct was inherently unlawful, Apple could be tagged with having "agreed to the horizontal restraint," App. 61a, and held liable *per se* because it supposedly knew that its vertical actions would allow the publishers to accomplish their goal of raising retail prices for certain e-books above Amazon's below-cost $9.99 price point. App. 44a-50a. But vertical conduct—especially concededly lawful vertical conduct with obviously legitimate aims and the potential for procompetitive benefits—may not be relabeled as a "horizontal price fixing-conspiracy" merely because it is claimed to have facilitated a horizontal conspiracy.

In *Business Electronics*, this Court rejected the proposition that a restraint between parties at different levels of the industry structure should be treated as "a horizontal rather than a vertical restraint" (and thus as *per se* illegal) merely because it would restrain horizontal "dealer-level competition." 485 U.S. at 729, 730. As that case makes clear, it is error to determine "whether a restraint is horizontal" based on "whether its anticompetitive *effects* are horizontal." *Id.* at 730 n.4. Rather, "a restraint is horizontal not because it has horizontal effects, but because it is the product of a horizontal agreement." *Id.* at 731 n.4. Thus, "[r]estraints imposed by agreement between competitors have traditionally been denominated as horizontal restraints, and those imposed by agreement between firms at different levels of distribution as vertical." *Id.* at 730.

Indeed, if courts could relabel vertical activities as *per se* illegal horizontal conduct merely because they allegedly impeded competition among horizontal rivals, this Court's directives that resale price maintenance (*Leegin*) and territorial restrictions (*Sylvania*) be assessed under the rule of reason would be nullified. Resale price maintenance would become "facilitation" of dealer price fixing, and territorial restraints would be transformed into "orchestration" of dealer market division. *Business Elecs.*, 485 U.S. at 730 n.4 (observing that if agreements were classified as horizontal based on their horizontal effects, there would be no such thing as an illegal vertical agreement). For example, the panel majority and the district court repeatedly characterized Apple's vertical conduct as having "eliminated retail price competition" through introduction of the agency-plus-MFNs business model, citing supposed price effects as a basis for *per se* condemnation of Apple's vertical conduct. *E.g.*, App. 36a, 127a-128a. But *Leegin* involved a challenge to vertical agreements *expressly intended* to eliminate competitive discounting by retailers; that is precisely what resale price maintenance agreements are designed to do. 551 U.S. at 882-883; *see also Sylvania*, 433 U.S. at 57-59.

This Court's insistence on carefully distinguishing between vertical and horizontal conduct stems from the same imperative that drove *Leegin*, *Khan*, and *Sylvania*: ensuring that courts do not chill procompetitive vertical conduct through *per se* condemnation. *E.g.*, *Business Elecs.*, 485 U.S. at 726. If vertical activity is alleged to have facilitated horizontal collusion, any resulting anticompetitive effects factor into the rule-of-reason assessment, along with the vertical conduct's procompetitive benefits. *See, e.g.*, *Toledo Mack*, 530 F.3d at 225 & n.15; *see also, e.g.*, *In re Southeastern Milk Antitrust Litig.*, 739 F.3d 262, 273 (6th Cir. 2014) (where "the restraint at issue appears to involve a vertical relationship," the court is required "to apply the rule of reason").

Here, though, the panel majority ignored the vertical character of Apple's conduct. Much of that conduct involved proposing and negotiating the terms of vertical contracts, and was therefore vertical by definition. *E.g.*, App. 57a, 228a. Apple's vertical agency agreements were themselves unquestionably procompetitive; they brought Apple into the e-books market to disrupt single-firm dominance. *See United States* v. *General Elec. Co.*, 272 U.S. 476, 488 (1926) ("genuine contracts of agency" are not "violations of the Anti-Trust Act"). Holding Apple liable *per se* for having facilitated a horizontal price-fixing conspiracy because its vertical agreements allowed the publishers to increase prices, *e.g.*, App. 66a, was error; "all vertical restraints … have the potential to allow [the price-setters] to increase 'prices' and can be characterized as intended to achieve just that," *Business Elecs.*, 485 U.S. at 728.

The few other purported incidents that the panel majority believed demonstrated Apple's "orchestrat[ion of] a horizontal conspiracy among" the publishers, App. 4a, similarly provide no basis to relabel Apple's vertical conduct as horizontal. For example, the majority pointed to Apple's purportedly encouraging two publishers to convince a third that it should agree to Apple's agency terms and join the iBookstore, App. 23a-25a, and to Apple's "'ke[eping] the [publishers] apprised about who was in and how many were on board,'" App. 26a; *see also* App. 28a-29a, 48a-49a. But Apple indisputably undertook those actions to assemble the critical mass of suppliers necessary to launch the iBookstore and bring competition to a market that desperately needed it. And more broadly, Apple's courting of the publishers and discussions about their needs—including pointing out that new competition from the iBookstore could give the publishers sufficient leverage to move Amazon from the below-cost pricing model that harmed them—were entirely proper aspects of Apple's efforts to launch a new content platform. As this Court has found, back-and-forth between manufacturers and distributors is "legitimate," "natural," and "'arise[s] in the normal course of business and do[es] not indicate illegal concerted action.'" *Monsanto Co.* v. *Spray-Rite Serv. Corp.*, 465 U.S. 752, 763 (1984). Indeed, "expos[ing] [a] defendant to treble damage liability"—much less *per se* condemnation—because it responds to input from vertical counterparties and crafts its business proposition accordingly "would create an irrational dislocation in the market," "'inhibit management's exercise of independent business judgment[,] and emasculate the terms of the [Sherman Act].'" *Id.* at 763, 764.[9]

[9] In recasting Apple's vertical conduct as orchestration of horizontal collusion among publishers, the courts below also relied on Apple's observations about the likely effects of its market entry, such as telling publishers that joining the iBookstore was their best chance to move Amazon off its loss-leader pricing, or responding to the publishers' justifiable fear that Amazon would retaliate against any single publisher who signed on to Apple's agency model. *E.g.*, App. 23a, 216a-217a, 240a; *see also, e.g.* App. 190a-191a (relying on purported prediction that Amazon's $9.99 price would not persist). Such statements of the obvious or efforts to persuade potential suppliers regarding the benefits of a new platform cannot

The courts below also continually and mistakenly invoked alleged short-term price increases for certain e-books in condemning Apple's conduct as *per se* illegal, *E.g.*, App. 66a-69a, 127a-129a, 219a-220a, failing to recognize that "prices can be increased in the course of promoting procompetitive effects," *Leegin*, 551 U.S. at 895-896. They confused the pricing decisions of a single dominant firm with the operation of the competitive *process*. That a monopolist has "cut[] prices to unsustainably low levels—prices below 'incremental' costs"—does not signify healthy competition. *Barry Wright Corp.* v. *ITT Grinnell Corp.*, 724 F.2d 227, 231 (1st Cir. 1983) (Breyer, J.); *see also Brooke Group Ltd.* v. *Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 237 (1993). If a new firm's entry disrupts a monopoly and creates long-term competition, that is to be lauded, whether the previous prices were artificially high or artificially low. *See Sommers* v. *Apple, Inc.*, 729 F.3d 953, 964 (9th Cir. 2013). Purported price increases are no justification for ignoring the difference between vertical and horizontal conduct and subjecting vertical conduct to *per se* condemnation.

The panel majority's conflation of Apple's vertical conduct with its purported horizontal effects ignores this Court's teaching that "easy labels do not always supply ready answers." *Broadcast Music*, 441 U.S. at 8-9 (declining to condemn potentially procompetitive conduct that was "'price fixing' in the literal sense" as *per se* illegal); *see also Northwest Wholesale Stationers*,

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justify *per se* treatment. Applying the *per se* rule based on inferences from such regular business remarks would "deter or penalize perfectly legitimate conduct" and "seriously erode[]" rules crafted to support procompetitive vertical conduct. *Monsanto*, 465 U.S. at 763.

Inc. v. *Pacific Stationery & Printing Co.*, 472 U.S. 284, 293-297 (1985) (refusing to condemn as *per se* illegal conduct that could be labeled a "group boycott" but lacked obvious anticompetitive effects). And the majority's resulting use of the *per se* rule disregards this Court's insistence that "'departure from the rule-of-reason standard … be based on demonstrable economic effect rather than upon formalistic line drawing.'" *Leegin*, 551 U.S. at 887.

2. The panel majority invoked "hub-and-spoke" cases, App. 55a-58a, but those cases do not support application of the *per se* rule here. Those cases, all of which predate *Leegin*, involved a "hub" firm that actively shepherded an agreement among horizontal competitors (the "spokes") for the *exclusive* purpose of illegally boycotting or otherwise undermining rivals to achieve a patently illegal objective. They are naked group-boycott cases where the hub's actions lacked *any* potential redeeming virtue and (unlike Apple's conduct here) were not in pursuit of a procompetitive objective, like assembling suppliers for a content platform. *See California Dental Ass'n* v. *FTC*, 526 U.S. 756, 771 (1999) (summary condemnation improper where challenged conduct might "plausibly be thought to have a net procompetitive effect").

For example, in *Klor's, Inc.* v. *Broadway-Hale Stores, Inc.*, the hub, a dominant retailer, organized a group boycott by its suppliers to deprive a small competing retailer of "its freedom to buy appliances in an open competitive market and drive[] it out of business as a dealer in the [suppliers'] products." 359 U.S. 207, 213 (1959). Similarly, in *Toys "R" Us, Inc.* v. *FTC*, a dominant toy retailer bullied its suppliers into refusing to deal or dealing only on unfavorable terms with competing retailers. 221 F.3d 928, 935-936 (7th Cir. 2000).

And notably, before upholding liability under the *per se* rule, the Seventh Circuit in *Toys "R" Us* considered whether the retailer's conduct was in pursuit of a non-pretextual procompetitive objective—avoiding free-riding—and found that it was not. *Id.* at 937-938. That is precisely the question the Second Circuit should have asked here, but never did.

In other cases on which the panel majority relied, horizontal competitors enlisted a hub supplier to act for the sole purpose of organizing and enforcing the horizontal competitors' collusive boycotting of rivals. *See United States* v. *General Motors Corp.*, 384 U.S. 127, 139-141 (1966) (Chevrolet dealers and dealer associations enlisted hub GM in effort to "eliminate" discount sellers "by terminating business dealings" with them, using GM to monitor and enforce dealers' horizontal agreement); *Denny's Marina, Inc.* v. *Renfro Prods., Inc.*, 8 F.3d 1217, 1219-1220 (7th Cir. 1993) (rival boat dealers and boat dealer association forced boat show producer to exclude competing dealer). None of those cases involved bona fide vertical activity with genuine procompetitive aims. Instead, they involved predatory conduct that was merely "facially vertical" and aimed solely at an unlawful objective like eliminating an incipient rival. *Business Elecs.*, 485 U.S. at 731 n.4; *see also Sylvania*, 433 U.S. at 58 n.28 (*General Motors* involved "horizontal restrictions originating in agreements among the [competing] retailers" rather than true vertical restrictions).

Here, by contrast, Apple was undisputedly engaged in vertical dealings with the publishers to advance its own "independent, economic interests," App. 227a; *see also* App. 47a, in bringing competition to the e-books market. *See, e.g., U.S. Healthcare, Inc.* v. *Healthsource, Inc.*, 986 F.2d 589, 593-594 (1st Cir. 1993) (rejecting *per se* liability premised on exclusive-dealing clauses alleged to have facilitated horizontal conspiracy and observing that clauses served vertically-situated firm's "own interests"). Of course, Apple acted as an organizer in the sense that it was developing a content platform, which required it to sign up multiple suppliers for that new venture. But that sort of procompetitive organizing is categorically different from the naked exclusionary conduct at issue in *Klor's*, *General Motors*, and *Toys "R" Us*.

Finally, because the panel majority's hub-and-spoke cases all predate *Leegin* (many predate *Khan* and *Sylvania* too), the courts in those cases did not have the benefit of *Leegin*'s guidance regarding the critical importance of distinguishing vertical from horizontal conduct and evaluating vertical conduct under the rule of reason. *Cf. Musical Instruments*, 798 F.3d at 1192-1193 (evaluating ostensible "hub-and-spoke" conspiracy post-*Leegin*).

II. THE QUESTION PRESENTED IS EXCEEDINGLY IMPORTANT TO THE NATIONAL ECONOMY

Whether the *per se* rule applies to novel, vertical business arrangements is a question of exceptional importance to businesses, innovators, and the national economy. The Second Circuit's rule threatens market entrants and risk-takers with unpredictable summary condemnation of vertical conduct in pursuit of procompetitive objectives. Unless reversed, the panel majority's conception of the *per se* rule will sow uncertainty, discourage procompetitive business ventures, and chill innovation and risk taking to the benefit of entrenched incumbents and the detriment of consumers.[10]

A. The decision below creates great uncertainty about the demarcation between lawful vertical conduct and *per se* illegal facilitation of a horizontal conspiracy. That vagueness makes it perilously difficult for market participants to tell when vertical conduct might cross a line into *per se* condemnation—and will result in substantial chilling of procompetitive endeavors.

The panel majority's expansive notion of *per se* liability could reach all manner of legitimate vertical conduct whenever a company becomes enmeshed with some form of alleged collusion, if only because of the business necessities of assembling suppliers at a different industry level. Apple's situation illustrates the point. Its goal was to enter the e-books market and compete against Amazon, and it developed a new vertical business model to do so. Because Apple needed a critical mass of suppliers to launch the iBookstore, it told publishers that it would enter the market only if a minimum number of them signed agency agreements and kept them apprised of how many had done so.

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[10] The question presented is also outcome-determinative in this case. *See* App. 90a (Lohier, J., concurring) ("Apple's appeal rises or falls based on the application of the per se rule."). Although neither the district court nor the panel majority applied a proper rule-of-reason analysis, there is every reason to believe that Apple's conduct in bringing competition to a monopolized market would survive such an assessment, as Judge Jacobs explained. *E.g.*, App. 110a-116a. Even the district court, although ruling against Apple in a cursory, one-paragraph rule-of-reason analysis (that was not affirmed), App. 219a-220a, acknowledged that "having the creativity and commitment of Apple invested in the enhancement of a product like the iBookstore [was] extremely beneficial to consumers and competition," App. 248a n.69.

The decision below rests on the assumption that, at some point, Apple's knowledge of the publishers' goals related to the deal—their desire to move Amazon off its loss-leader $9.99 price—should have caused Apple to abandon its otherwise lawful attempts at entry, lest it risk *per se* condemnation under the antitrust laws (and treble damages). *Contra Monsanto*, 465 U.S. at 763-764. That assumption gives future entrants no guidance as to when legitimate vertical business dealings might cross the *per se* line. Was Apple supposed to abandon the iBookstore because the terms that allowed it to enter the market might also have helped the publishers accomplish their separate goal of moving Amazon to a different business model? Was Apple supposed to abandon the iBookstore—and leave Amazon's dominance undisturbed—if it developed some quantum of suspicion that the publishers were colluding among themselves?

Absent this Court's review, the line dividing legal and *per se* illegal conduct will be blurred, in contravention of this Court's "repeated[] emphasi[s] [on] the importance of clear rules in antitrust law." *Pacific Bell Tel. Co.* v. *Linkline Commc'ns, Inc.*, 555 U.S. 438, 452 (2009); *see also FCC* v. *Fox Television Stations, Inc.*, 132 S. Ct. 2307, 2317 (2012) (it is a "fundamental principle in our legal system … that laws which regulate persons or entities must give fair notice of conduct that is forbidden"); *Town of Concord* v. *Boston Edison Co.*, 915 F.2d 17, 22 (1st Cir. 1990) (Breyer, J.) ("antitrust rules … must be clear enough for lawyers to explain them to clients"). Instead, firms—including incipient platform suppliers and digital innovators—will constantly fear that their otherwise lawful vertical conduct will result in treble damages and will be forced to curb their entrepreneurship accordingly.

B. The uncertainty engendered by the decisions below will also discourage vertical contracting provisions that frequently serve important procompetitive purposes. Vertical terms tailored to the demands of the particular circumstances—*e.g.*, terms addressing parties' incongruent incentives (like those here)—are often necessary to permit disruptive entry into new or stagnant markets. *Leegin*, 551 U.S. at 891 (resale price maintenance can "facilitat[e] market entry for new firms and brands"). Such terms can "encourage[] retailers to invest in tangible or intangible services or promotional efforts" and have "the potential to give consumers more options." *Id.* at 890. And parallel vertical arrangements are absolutely crucial to new entry in the digital economy.[11]

Yet under the Second Circuit's approach, new entrants justifiably will fear that their particular form of vertical dealing could be declared *per se* unlawful without inquiry into overall context and market effects, even if it would withstand scrutiny under the rule of reason.

For example, the panel majority's decision creates great uncertainty as to whether and when a vertical player may use MFN clauses. The Second Circuit condemned the MFN clauses for allegedly "'stiffen[ing] the spines'" of the publishers to demand agency terms from Amazon. App. 45a. But as the courts below recognized, MFN clauses are not inherently anticompetitive. *E.g.*, App. 228a. That is not changed by the fact an

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[11] E-commerce platforms that aggregate inputs from disparate suppliers have become ubiquitous and are a driver of American prosperity—from product retailers like Amazon and eBay, to content platforms like Netflix, iTunes, and YouTube, to sharing economy platforms like Uber and Airbnb.

MFN in an agency agreement may have the effect of eliminating price competition among retailers and vesting it instead with product suppliers. *See, e.g.*, *In re Online Travel Co. (OTC) Hotel Booking Antitrust Litig.*, 997 F. Supp. 2d 526, 538 (N.D. Tex. 2014) (rejecting characterization of MFN clauses in agency agreements as *per se* illegal price-fixing and observing that MFN clauses serve the legitimate purpose of ensuring that retailers "will not be undercut").

Here, Apple needed the MFN clauses to "protect[] [its] interests" against the publishers' potentially adverse interests. App. 157a; *see, e.g.*, *Sulfuric Acid*, 703 F.3d at 1012 (*per se* rule did not apply to new entrant's agreements with existing suppliers because "the aim was to facilitate entry into the U.S. market"). Indeed, MFN provisions in agency agreements are particularly common in the world of e-commerce. Weiner & Falls, *Counseling on MFNs After* e-books, 28 Antitrust 68, 69 (Summer 2014) ("[P]rice parity MFNs arising in an agency model of distribution … are increasingly being used in e-commerce by online selling platforms.").

By applying the *per se* rule to Apple's vertical activity, the panel majority committed an "especially costly" mistake, "chill[ing] the very conduct the antitrust laws are designed to protect." *Matsushita Elec. Indus. Co.* v. *Zenith Radio Corp.*, 475 U.S. 574, 594 (1986); *see also United States* v. *U.S. Gypsum Co.*, 438 U.S. 422, 441-442 n.17 (1978) ("The possibility that those subjected to strict liability will take extraordinary care in their dealings is frequently regarded as one advantage of a rule of strict liability. However, where the conduct proscribed is difficult to distinguish from conduct permitted and indeed encouraged, as in the antitrust context, the excessive caution spawned by a regime of strict liability will not necessarily redound to the public's benefit." (citations omitted)). Particularly for market entry—the very essence of competition—new entrants like Apple must have flexibility to use vertical tools to address contracting challenges without risking *per se* antitrust liability. *See Sulfuric Acid*, 703 F.3d at 1012 ("The plaintiffs' claim that the price would have been even lower without the [challenged price-raising] agreements is doubtful … because without the agreements the [defendants] might not have entered the U.S. market."); *see also Leegin*, 551 U.S. at 917-918 (Breyer, J., dissenting) (discussing potential "exception" to *per se* rule for resale price maintenance to facilitate new entry). At bottom, Apple offered suppliers an appealing new vertical business model in order to facilitate its entry into the market; the Second Circuit's decision cuts deep into territory that this Court's modern antitrust decisions have sought to protect from *per se* condemnation precisely because of vertical conduct's procompetitive potential.

The panel majority was unconcerned about "stifl[ing] productive enterprise" by inferring a *per se* unlawful price-fixing agreement on the basis of otherwise lawful vertical conduct; in its view, "vertical agreements, lawful in the abstract, can in context 'be useful evidence for … attempting to prove the existence of a horizontal cartel,' particularly where multiple competitors sign vertical agreements that would be against their own interests were they acting independently." App. 50a, 51a (citing *Toys "R" Us*, 221 F.3d at 935-936, and *Interstate Circuit, Inc.* v. *United States*, 306 U.S. 208, 222 (1939)). This reasoning illustrates the risk of deterring procompetitive vertical contracting. Apple's object was to launch a *multi*-publisher content platform that required a critical mass to be viable; the nature of such platforms meant that each publisher's determination whether joining served its own interests *necessarily* depended on the decisions of other publishers. That Apple recognized this interdependence and used it in successfully launching the iBookstore does not make its efforts to enter the market *per se* illegal.

C. Entry into new markets and disruption of established business models through innovation are critical to the American economy, especially in new and rapidly growing markets for digital products and services. If the Second Circuit's decision stands and the *per se* rule is applied to vertical conduct whenever it can be said to have spilled over into "orchestration" of others' alleged horizontal collusion, the antitrust laws will be transformed from a tool for promoting new entry and competition into a means for retarding them. Entrants and disruptors will err on the side of staying out of new markets and will forgo the types of vertical contracting that are so often necessary for entry, thus leaving dominant players protected from the disruptive challenges that drive innovation. Those outcomes are antithetical to the dynamic and robust competitive environment that our antitrust laws are meant to foster. *See, e.g.*, *United States* v. *Aluminum Co. of Am.*, 148 F.2d 416, 427 (2d Cir. 1945) (L. Hand, J.) ("[I]mmunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress.").

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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OCTOBER 2015

APPENDIX

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Nos. 13-3741-cv, 13-3748-cv, 13-3783-cv, 13-3857-cv, 13-3864-cv, 13-3867-cv

Argued: December 15, 2014
Decided: June 30, 2015
(as amended July 2, 1015)

UNITED STATES OF AMERICA, STATE OF TEXAS, STATE OF CONNECTICUT, STATE OF ALABAMA, STATE OF ALASKA, STATE OF ARIZONA, STATE OF ARKANSAS, STATE OF COLORADO, STATE OF DELAWARE, STATE OF IDAHO, STATE OF ILLINOIS, STATE OF INDIANA, STATE OF IOWA, STATE OF KANSAS, STATE OF LOUISIANA, STATE OF MARYLAND, COMMONWEALTH OF MASSACHUSETTS, STATE OF MICHIGAN, STATE OF MISSOURI, STATE OF NEBRASKA, STATE OF NEW MEXICO, STATE OF NEW YORK, STATE OF NORTH DAKOTA, STATE OF OHIO, COMMONWEALTH OF PENNSYLVANIA, STATE OF SOUTH DAKOTA, STATE OF TENNESSEE, STATE OF UTAH, STATE OF VERMONT, COMMONWEALTH OF VIRGINIA, STATE OF WEST VIRGINIA, STATE OF WISCONSIN, COMMONWEALTH OF PUERTO RICO, AND DISTRICT OF COLUMBIA,
Plaintiffs-Appellees,

v.

APPLE, INC., SIMON & SCHUSTER, INC., VERLAGSGRUPPE GEORG VON HOLTZBRINCK GMBH, HOLTZBRINCK PUBLISHERS, LLC, DBA MACMILLAN, SIMON & SCHUSTER DIGITAL SALES, INC.,
Defendants-Appellants,

HACHETTE BOOK GROUP, INC., HARPERCOLLINS PUBLISHERS L.L.C., THE PENGUIN GROUP, A DIVISION OF PEARSON PLC, PENGUIN GROUP (USA), INC.,
Defendants.

Before: JACOBS, LIVINGSTON, and LOHIER, *Circuit Judges*.

* * *

[4] DEBRA ANN LIVINGSTON, *Circuit Judge*:

Since the invention of the printing press, the distribution of books has involved a fundamentally consistent process: compose a manuscript, print and bind it into physical volumes, and then ship and sell the volumes to the public. In late 2007, Amazon.com, Inc. ("Amazon") introduced the Kindle, a portable device that carries digital copies of books, known as "ebooks." This innovation had the potential to change the centuries-old process for producing books by eliminating the need to print, bind, ship, and store them. Amazon began to popularize the new way to read, and encouraged consumers to buy the Kindle by offering desirable books—new releases and *New York Times* bestsellers—for $9.99. Publishing companies, which have traditionally stood at the center of the [5] multi-billion dollar book-producing industry, saw Amazon's ebooks, and particularly its $9.99 pricing, as a threat to their way of doing business.

By November 2009, Apple, Inc. ("Apple") had plans to release a new tablet computer, the iPad. Executives at the company saw an opportunity to sell ebooks on the iPad by creating a virtual marketplace on the device, which came to be known as the "iBookstore." Working within a tight timeframe, Apple went directly into negotiations with six of the major publishing companies in the United States. In two months, it announced that five of those companies—Hachette, Harpercollins, Macmillan, Penguin, and Simon & Schuster (collectively, the "Publisher Defendants")—had agreed to sell ebooks on the iPad under arrangements whereby the publishers had the authority to set prices, and could set the prices of new releases and *New York Times* bestsellers as high as $19.99 and $14.99, respectively. Each of these agreements, by virtue of its terms, resulted in each Publisher Defendant receiving *less* per ebook sold via Apple as opposed to Amazon, even given the higher consumer prices. Just a few months after the iBookstore opened, however, every one of the Publisher Defendants had taken control over pricing from Amazon and had raised the prices on many of their ebooks, most notably new releases and bestsellers.

[6] The United States Department of Justice ("DOJ" or "Justice Department") and 33 states and territories (collectively, "Plaintiffs") filed suit in the United States District Court for the Southern District of New York, alleging that Apple, in launching the iBookstore, had conspired with the Publisher Defendants to raise prices across the nascent ebook market. This agreement, they argued, violated § 1 of the Sherman Antitrust Act, 15 U.S.C. § 1 *et seq.* ("Sherman Act"), and state antitrust laws. All five Publisher Defendants settled and signed consent decrees, which prohibited them, for a period, from restricting ebook retailers' ability to set prices. Then, after a three-week bench trial, the district court (Cote, *J.*) concluded that, in order to induce the Publisher Defendants to participate in the iBookstore and to avoid the necessity of itself competing with Amazon over the retail price of ebooks, Apple orchestrated a conspiracy among the Publisher Defendants to raise the price of ebooks—particularly new releases and *New York Times* best-sellers. *United States v. Apple Inc.*, 952 F. Supp. 2d 638, 647 (S.D.N.Y. 2013). The district court found that the agreement constituted a *per se* violation of the Sherman Act and, in the alternative, unreasonably restrained trade under the rule of reason. *See id.* at 694. On September 5, 2013, the district court entered final judgment on the liability finding and issued an injunctive [7] order that, *inter alia*, prevents Apple from entering into agreements with the Publisher Defendants that restrict its ability to set, alter, or reduce the price of ebooks, and requires Apple to apply the same terms and conditions to ebook applications sold on its devices as it does to other applications.

On appeal, Apple contends that the district court's liability finding was erroneous and that the provisions of the injunction related to its pricing authority and ebook applications are not necessary to protect the public. Two of the Publisher Defendants—Macmillan and Simon & Schuster—join the appeal, arguing that the portion of the injunction related to Apple's pricing authority either unlawfully modifies their consent decrees or should be judicially estopped. We conclude that the district court's decision that Apple orchestrated a horizontal conspiracy among the Publisher Defendants to raise ebook prices is amply supported and well-reasoned, and that the agreement unreasonably restrained trade in violation of § 1 of the Sherman Act. We also conclude that the district court's injunction is lawful and consistent with preventing future anticompetitive harms.

Significantly, the dissent *agrees* that Apple intentionally organized a conspiracy among the Publisher

Defendants to raise ebook prices. Nonetheless, [8] it contends that Apple was entitled to do so because the conspiracy helped it become an ebook retailer. In arriving at this startling conclusion—based in large measure on an argument that Apple itself did not assert—the dissent makes two fundamental errors. The first is to insist that the vertical organizer of a horizontal price-fixing conspiracy may escape application of the *per se* rule. This conclusion is based on a misreading of Supreme Court precedent, which establishes precisely the opposite. The dissent fails to apprehend that the Sherman Act outlaws *agreements* that unreasonably restrain trade and therefore requires evaluating the nature of the restraint, rather than the identity of each party who joins in to impose it, in determining whether the *per se* rule is properly invoked. Finally (and most fundamentally) the dissent's conclusion rests on an erroneous premise: that one who organizes a horizontal price-fixing conspiracy—the "supreme evil of antitrust," *Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 408 (2004)—among those competing at a different level of the market has somehow done less damage to competition than its co-conspirators.

The dissent's second error is to assume, in effect, that Apple was entitled to enter the ebook retail market on its own terms, even if these terms could be [9] achieved only via its orchestration of and entry into a price-fixing agreement with the Publisher Defendants. The dissent tells a story of Apple organizing this price-fixing conspiracy to rescue ebook retailers from a monopolist with insurmountable retail power. But this tale is not spun from any factual findings of the district court. And the dissent's armchair analysis wrongly treats the number of ebook retailers at any moment in the emergence of a new and transformative technology for book distribution as the *sine qua non* of competition in the market for trade ebooks.

More fundamentally, the dissent's theory—that the presence of a strong competitor justifies a horizontal price-fixing conspiracy—endorses a concept of marketplace vigilantism that is wholly foreign to the antitrust laws. By organizing a price-fixing conspiracy, Apple found an easy path to opening its iBookstore, but it did so by ensuring that market-wide ebook prices would rise to a level that it, and the Publisher Defendants, had jointly agreed upon. Plainly, competition is not served by permitting a market entrant to *eliminate price competition* as a condition of entry, and it is cold comfort to consumers that they gained a new ebook retailer at the expense of passing control over all ebook prices to a cartel of book publishers—publishers who, with Apple's help, **[10]** collectively agreed on a new pricing model precisely to *raise* the price of ebooks and thus protect their profit margins and their very existence in the marketplace in the face of the admittedly strong headwinds created by the new technology.

Because we conclude that the district court did not err in deciding that Apple violated § 1 of the Sherman Act, and because we also conclude that the district court's injunction was lawful and consistent with preventing future anticompetitive harms, we affirm.

BACKGROUND

I. Factual Background[1]

We begin not with Kindles and iPads, but with printed "trade books," which are "general interest fiction and non-fiction" books intended for a broad readership. *Apple*, 952 F. Supp. 2d at 648 n.4. In the United States, the six largest publishers of trade books, known in the publishing world as the "Big Six," are Hachette, HarperCollins, Macmillan, Penguin, Random House, and Simon & [11] Schuster. Together, the Big Six publish many of the biggest names in fiction and non-fiction; during 2010, their titles accounted for over 90% of the *New York Times* bestsellers in the United States. *Id.* at 648 n.5.

For decades, trade book publishers operated under a fairly consistent business model. When a new book was ready for release to the public, the publisher would sell hardcover copies to retailers at a "wholesale" price and recommend resale to consumers at a markup, known as the "list" price. After the hardcover spent enough time on the shelves—often a year—publishers would release a paperback copy at lower "list" and "wholesale" prices. In theory, devoted readers would pay the higher hardcover price to read the book when it

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[1] The factual background presented here is drawn from the district court's factual findings or from undisputed material in the record before the district court. Because this Court reviews the district court's factual findings for "clear error," we must assess whether "its view of the evidence is plausible in light of the entire record." *Cosme v. Henderson*, 287 F.3d 152, 158 (2d Cir. 2002). In light of this obligation, the dissent is wrong to suggest that citations to the record are inappropriate or misleading. When a fact comes from the district court's opinion, we cite that opinion; when one comes from the record, we cite the joint appendix ("J.A.").

first came out, while more casual fans would wait for the paperback.

A. Amazon's Kindle

On November 19, 2007, Amazon released the Kindle: a portable electronic device that allows consumers to purchase, download, and read ebooks. At the time, there was only one other ereader available in the emerging ebook market, and Amazon's Kindle quickly gained traction. In 2007, ebook revenue in North America was only $70 million, a tiny amount relative to the approximately $30 billion market for physical trade books. The market was growing, however; in [12] 2008 ebook revenue was roughly $140 million and, by the time Barnes & Noble, Inc. (Barnes & Noble) launched its Nook ereader in November 2009, Amazon was responsible for 90% of all ebook sales. *Apple*, 952 F. Supp. 2d at 648-49.

Amazon followed a "wholesale" business model similar to the one used with print books: publishers recommended a digital list price and received a wholesale price for each ebook that Amazon sold. In exchange, Amazon could sell the publishers' ebooks on the Kindle and determine the retail price. At least early on, publishers tended to recommend a digital list price that was about 20% lower than the print list price to reflect the fact that, with an ebook, there is no cost for printing, storing, packaging, shipping, or returning the books.

Where Amazon departed from the publishers' traditional business model was in the sale of new releases and *New York Times* bestsellers. Rather than selling more expensive versions of these books upon initial release (as publishers encouraged by producing hardcover books before paperback copies), Amazon set the

Kindle price at one, stable figure—$9.99. At this price, Amazon was selling "certain" new releases and bestsellers at a price that "roughly matched," or was slightly lower than, the wholesale price it paid to the publishers. *Apple*, 952 F. Supp. 2d at 649. David Naggar, a Vice President in charge of Amazon's **[13]** Kindle content, described this as a "classic loss-leading strategy" designed to encourage consumers to adopt the Kindle by discounting new releases and *New York Times* bestsellers and selling other ebooks without the discount. J.A. 1485. The district court also referred to this as a "loss leader[]" strategy, *Apple*, 952 F.5 Supp. 2d at 650, 657, 708, and explained that Amazon "believed [the $9.99] pricing would have long-term benefits for its consumers," *id.* at 649. Contrary to the dissent's portrayal of the opinion, 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. Dissenting Op. at 6-7. Indeed, in November 2009—just a few months before Apple's launch of the iBookstore—Barnes & Noble entered the ebook retail market by launching the Nook, *Apple*, 952 F. Supp. 2d at 649 n.6, and as early as 2007 Google Inc. ("Google") had been planning to enter the market using a wholesale model, *id.* at 686.

B. The Publishers' Reactions

Despite the small number of ebook sales compared to the overall market for trade books, top executives in the Big Six saw Amazon's $9.99 pricing strategy as a threat to their established way of doing business. Those executives **[14]** included: Hachette and Hachette Livre Chief Executive Officers ("CEOs") David Young and Arnaud Nourry; HarperCollins CEO Brian Murray; Macmillan CEO John Sargent; Penguin

USA CEO David Shanks; Random House Chief Operating Officer Madeline McIntosh; and Simon & Schuster President and CEO Carolyn Reidy. In the short term, these members of the Big Six thought that Amazon's lower-priced ebooks would make it more difficult for them to sell hardcover copies of new releases, "which were often priced," as the district court noted, "at thirty dollars or more," *Apple*, 952 F. Supp. 2d at 649, as well as *New York Times* bestsellers. Further down the road, the publishers feared that consumers would become accustomed to the uniform $9.99 price point for these ebooks, permanently driving down the price they could charge for print versions of the books. Moreover, if Amazon became powerful enough, it could demand lower wholesale prices from the Big Six or allow authors to publish directly with Amazon, cutting out the publishers entirely. As Hachette's Young put it, the idea of the "wretched $9.99 price point becoming a de facto standard" for ebooks "sickened" him. J.A. 289.

The executives of the Big Six also recognized that their problem was a collective one. Thus, an August 2009 Penguin strategy report (concluded only a **[15]** few months before Apple commenced its efforts to launch the iBookstore) noted that "[c]ompetition for the attention of readers will be most intense from digital companies whose objective may be to [cut out] traditional publishers altogether.... It will not be possible for any individual publisher to mount an effective response, because of both the resources necessary and the risk of retribution, so the industry needs to develop a common strategy." J.A. 287. Similarly, Reidy from Simon & Schuster opined in September 2009 that the publishers had "no chance of success in getting Amazon to change its pricing practices" unless they acted with a "critical mass," and expressed the "need to gather more troops and ammunition" before implementing a move against Amazon. J.A. 290 (internal quotation marks omitted).

Conveniently, the Big Six operated in a close-knit industry and had no qualms communicating about the need to act together. As the district court found (based on the Publisher Defendants' own testimony), "[o]n a fairly regular basis, roughly once a quarter, the CEOs of the [Big Six] held dinners in the private dining rooms of New York restaurants, without counsel or assistants present, in order to discuss the common challenges they faced." *Apple*, 952 F.18 Supp. 2d at 651. Because they "did not compete with each other on price," but **[16]** over authors and agents, the publishers "felt no hesitation in freely discussing Amazon's prices with each other and their joint strategies for raising those prices." *Id.* Those strategies included eliminating the discounted wholesale price for ebooks and possibly creating an alternative ebook platform.

The most significant attack that the publishers considered and then undertook, however, was to withhold new and bestselling books from Amazon until the hardcover version had spent several months in stores, a practice known as "windowing." Members of the Big Six both kept one another abreast of their plans to window, and actively pushed others toward the strategy.[2]

[2] Citing one example, the district court referenced a fall 2009 email in which Hachette's Young informed his colleague Nourry of Simon & Schuster's windowing plans, advising "[c]ompletely confidentially, Carolyn [Reidy] has told me that they [Simon & Schuster] are delaying the new Stephen King, with his full support, but will not be announcing this until the day after Labor Day." *Apple*, 952 F. Supp. 2d at 652 (first and second alterations in original) (internal quotation marks omitted). The district court went on to

By December 2009, the *Wall Street Journal* and *New York Times* were reporting that four of the Big Six had announced plans to delay ebook releases until after the print release, and the two holdouts—Penguin and Random House—faced pressure from their peers.

[17] Ultimately, however, the publishers viewed even this strategy to save their business model as self-destructive. Employees inside the publishing companies noted that windowing encouraged piracy, punished ebook consumers, and harmed long-term sales. One author wrote to Sargent in December 2009 that the "old model has to change" and that it would be better to "embrace e-books," publish them at the same time as the hardcovers, "and pray to God they both sell like crazy." J.A. 325. Sargent agreed, but expressed the hope that ebooks could eventually be sold for between $12.95 and $14.95. "The question is," he mused, "how to get there?" J.A. 325.

C. Apple's Entry into the Ebook Market

Apple is one of the world's most innovative and successful technology companies. Its hardware sells worldwide and supports major software marketplaces like iTunes and the App Store. But in 2009, Apple lacked a dedicated marketplace for ebooks or a hardware device that could offer an outstanding reading experience. The pending release of the iPad, which Apple intended to announce on January 27, 2010, promised to solve that hardware deficiency.

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observe that Young, "[u]nderstanding the impropriety of this exchange of confidential information with a competitor, … advised Nourry that 'it would be prudent for you to double delete this from your email files when you return to your office.'" *Id.*

[18] Eddy Cue, Apple's Senior Vice President of Internet Software and Services and the director of Apple's digital content stores, saw the opportunity for an ebook marketplace on the iPad. By February 2009, Cue and two colleagues—Kevin Saul and Keith Moerer—had researched the ebook market and concluded that it was poised for rapid expansion in 2010 and beyond. While Amazon had an estimated 90% market share in trade ebooks, Cue believed that Apple could become a powerful player in the market in large part because consumers would be able to do many tasks on the iPad, and would not want to carry a separate Kindle for reading alone. In an email to Apple's then-CEO, Steve Jobs, he discussed the possibility of Amazon selling ebooks through an application on the iPad, but felt that "it would be very easy for [Apple] to compete with and … trounce Amazon by opening up our own ebook store" because "[t]he book publishers would do almost anything for [Apple] to get into the ebook business." J.A. 282.

Jobs approved Cue's plan for an ebook marketplace—which came to be known as the iBookstore—in November 2009. Although the iPad would go to market with or without the iBookstore, Apple hoped to announce the ebook marketplace at the January 27, 2010 iPad launch to "ensure maximum consumer [19] exposure" and add another "dramatic component" to the event. *Apple*, 952 F. Supp. 2d at 655. This left Cue and his team only two months amidst the holiday season both to create a business model for the iBookstore and to assemble a group of publishers to participate. Cue also had personal reasons to work quickly. He knew that Jobs was seriously ill, and that, by making the iBookstore a success, he could help Jobs achieve a longstanding goal of creating a device that provides a superior reading experience.

Operating under a tight timeframe, Cue, Saul, and Moerer streamlined their efforts by focusing on the Big Six publishers. They began by arming themselves with some important information about the state of affairs within the publishing industry. In particular, they learned that the publishers feared that Amazon's pricing model could change their industry, that several publishers had engaged in simultaneous windowing efforts to thwart Amazon, and that the industry as a whole was in a state of turmoil. "Apple understood," as the district court put it, "that the Publishers wanted to pressure Amazon to raise the $9.99 price point for e-books, that the Publishers were searching for ways to do that, and that they were willing to coordinate their efforts to achieve that goal." *Id.* at 656. For its part, as the district court found, Apple was willing to sell ebooks at **[20]** higher prices, but "had decided that it would not open the iBookstore if it could not make money on the store and compete effectively with Amazon." *Id.*

D. Apple's Negotiations with the Publishers

1. Initial Meetings

Apple held its first meetings with each of the Big Six between December 15 and 16. The meetings quickly confirmed Cue's suspicions about the industry. As he wrote to Jobs after speaking with three of the publishers, "[c]learly, the biggest issue is new release pricing" and "Amazon is definitely not liked much because of selling below cost for NYT Best Sellers." J.A. 326-27. Many publishers also emphasized that they were searching for a strategy to regain control over pricing. Apple informed each of the Big Six that it was negotiating with the other major publishers, that it hoped to begin selling ebooks within the next 90 days, and that it was seeking a critical mass of participants in the iBookstore and would launch only if successful in reaching this goal. Apple informed the publishers that it did not believe the iBookstore would succeed unless publishers agreed both not to window books and to sell ebooks at a discount relative to their physical counterparts. Apple noted that ebook prices in the iBookstore needed to be comparable to those on the Kindle, expressing the view, as Reidy recorded, **[21]** that it could not "tolerate a market where the product is sold significantly more cheaply elsewhere." *Apple*, 952 F. Supp. 2d at 657 (internal quotation marks omitted). Most importantly for the publishers, however, Cue's team also expressed Apple's belief that Amazon's $9.99 price point was not ingrained in consumers' minds, and that Apple could sell new releases and *New York Times* bestsellers for somewhere between $12.99 and $14.99. In return, Apple requested that the publishers decrease their wholesale prices so that the company could make a small profit on each sale.

These meetings spurred a flurry of communications reporting on the "[t]errific news[,]" as Reidy put it in an email to Leslie Moonves, her superior at parent company CBS Corporation ("CBS"), that Apple "was not interested in a low price point for digital books" and didn't want "Amazon's $9.95 [sic] to continue." *Apple*, 952 F. Supp. 2d at 658 (first alteration in original) (internal quotation marks omitted). Significantly, these communications included numerous exchanges *between* executives at different Big Six publishers who, the district court found, "hashed over their meetings with Apple with one another." *Id.* The district court found that the frequent telephone calls among the Publisher **[22]** Defendants during the period of their negotiations with

Apple "represented a departure from the ordinary pattern of calls among them." *Id.* at 655 n.14.

2. The Agency Model

Meanwhile, Cue, Moerer, and Saul returned to Apple's headquarters to develop a business model for the iBookstore. Although the team was optimistic about the initial meetings, they remained concerned about whether the publishers would reduce wholesale prices on new releases and bestsellers by a large enough margin to allow Apple to offer competitive prices and still make a profit. One strategy that the team considered was to ask publishers for a 25% wholesale discount on all of these titles, so if a physical book sold at $12 wholesale (the going rate for the majority of *New York Times* bestsellers) Apple could purchase the ebook version for $9 and offer it on the iBookstore at a small markup. But Cue was aware that some publishers had increased Amazon's digital wholesale prices in 2009 in an unsuccessful effort to convince Amazon to change its pricing. *Id.* at 650; J.A. 1771. Cue felt it would be difficult to negotiate wholesale prices down far enough "for [Apple] to generally compete profitably with Amazon's below-cost pricing on the most popular e-books." J.A. 1772. As Cue saw it, Apple's most valuable bargaining chip came from the fact that the **[23]** publishers were desperate "for an alternative to Amazon's pricing policies and excited about … the prospect that [Apple's] entry [into the ebook market] would give them leverage in their negotiations with Amazon." *Apple*, 952 F. Supp. 2d at 659.

It was at this point that Cue's team, recognizing its opportunity, abandoned the wholesale business model for a new, agency model.[3] Unlike a wholesale model, in an agency relationship the *publisher* sets the price that consumers will pay for each ebook. Then, rather than the retailer paying the publisher for each ebook that it sells, the publisher pays the retailer a fixed percentage of each sale. In essence, the retailer receives a commission for distributing the publisher's ebooks. Under the system Apple devised, publishers would have the freedom to set ebook prices in the iBookstore, and would keep 70% of each sale. The remaining 30% would go to Apple as a commission.

This switch to an agency model obviated Apple's concerns about negotiating wholesale prices with the Big Six while ensuring that Apple profited on every sale. It did not, however, solve all of the company's problems. Because the agency model handed the publishers control over pricing, it created the risk **[24]** that the Big Six would sell ebooks in the iBookstore at far higher prices than Kindle's $9.99 offering. If the prices were too high, Apple could be left with a brand new marketplace brimming with titles, but devoid of customers.

To solve this pricing problem, Cue's team initially devised two strategies. First, they realized that they could maintain "realistic prices" by establishing price caps for different types of books. J.A. 359. Of course, these caps would need to be *higher* than Amazon's $9.99 price point, or Apple would face the same difficult price negotiations that it sought to avoid by switching away from the wholesale model. But at this point Apple was not content to open its iBookstore offering prices higher than the competition. For as the district court

[3] Notably, the possibility of an agency arrangement was first mentioned by Hachette and HarperCollins as a way "to fix Amazon pricing." J.A. 346.

found, if the Publisher Defendants "wanted to end Amazon's $9.99 pricing," Apple similarly desired "that there be no price competition at the retail level." *Apple*, 952 F. Supp. 2d at 647.

Apple next concluded, then, as the district court found, that "[t]o ensure that the iBookstore would be competitive at higher prices, Apple … needed to eliminate all retail price competition." *Id.* at 659. Thus, rather than simply agreeing to price caps above Amazon's $9.99 price point, Apple created a second requirement: publishers must switch all of their other ebook retailers—**[25]** including Amazon—to an agency pricing model. The result would be that Apple would not need to compete with Amazon on price, and publishers would be able to eliminate Amazon's $9.99 pricing. Or, as Cue would later describe the plan to executives at Simon & Schuster, Macmillan, and Random House, the plan "solve[d] [the] Amazon issue" by allowing the publishers to wrest control over pricing from Amazon.[4] *Id.* at 661 (internal quotation marks omitted).

On January 4 and 5, Apple sent essentially identical emails to each member of the Big Six to explain its agency model proposal. Each email described the commission split between Apple and the publishers and recommended three price caps: $14.99 for hardcover books with list prices above $35; $12.99 for hardcover

[4] Cue testified at trial that his reference to "solv[ing] the Amazon issue" denoted the proposal to price ebooks in the iBookstore above $9.99, and was not a reference to raising prices across the industry or wresting control over pricing from Amazon. In this and other respects, the district court found Cue's testimony to be "not credible"—a determination that, on this record, is in no manner erroneous, much less clearly so. *Id.* at 661 n.19. As the district court put it, "Apple's pitch to the Publishers was—from beginning to end—a vision for a new industry-wide price schedule." *Id.*

books with list prices below $35; and $9.99 for all other trade books. The emails also explained that, "to sell ebooks at realistic prices … all [other] resellers of new titles need to be in [the] agency model" as well. J.A. 360. Or, as Cue told Reidy, "all publishers" would need to move "all retailers" to an agency model. J.A. 2060.

[26]

3. The "Most-Favored-Nation" Clause

Cue's thoughts on the agency model continued to evolve after the emails on January 4 and 5. Most significantly, Saul—Cue's in-house counsel—devised an alternative to explicitly requiring publishers to switch other retailers to agency. This alternative involved the use of a "most-favored nation" clause ("MFN Clause" or "MFN"). In general, an MFN Clause is a contractual provision that requires one party to give the other the best terms that it makes available to any competitor. In the context of Apple's negotiations, the MFN Clause mandated that, "[i]f, for any particular New Release in hardcover format, the … Customer Price [in the iBookstore] at any time is or becomes higher than a customer price offered by any other reseller … , then [the] Publisher shall designate a new, lower Customer Price [in the iBookstore] to meet such lower [customer price]." J.A. 559. Put differently, the MFN would require the publisher to offer any ebook in Apple's iBookstore for no more than what the same ebook was offered elsewhere, such as from Amazon.

On January 11, Apple sent each of the Big Six a proposed eBook Agency Distribution Agreement (the "Contracts"). As described in the January 4 and 5 emails, these Contracts would split the proceeds from each ebook sale between **[27]** the publisher and Apple, with the publisher receiving 70%, and would set price caps on ebooks at $14.99, $12.99, and $9.99 depending on the book's hardcover price. But unlike the initial emails, the Contracts contained MFN Clauses in place of the requirement that publishers move all other retailers to an agency model. Apple then assured each member of the Big Six that it was being offered the same terms as the others.

The Big Six understood the economic incentives that the MFN Clause created. Suppose a new hardcover release sells at a list price of $25, and a wholesale price of $12.50. With Amazon, the publishers had been receiving the wholesale price (or a slightly lower digital wholesale price) for every ebook copy of the volume sold on Kindle, even if Amazon ultimately sold the ebook for less than that wholesale price. Under Apple's initial agency model—with price caps but no MFN Clause—the publishers already stood to make *less* money per ebook with Apple. Because Apple capped the ebook price of a $25 hardcover at $12.99 and took 30% of that price, publishers could only expect to make $8.75 per sale. But what the publishers sacrificed in short-term revenue, they hoped to gain in long-term stability by acquiring more control over pricing and, accordingly, the ability to protect their hardcover sales.

[28] The MFN Clause changed the situation by making it imperative, not merely desirable, that the publishers wrest control over pricing from ebook retailers generally. Under the MFN, if Amazon stayed at a wholesale model and continued to sell ebooks at $9.99, the publishers would be forced to sell in the iBookstore, too, at that same $9.99 price point. The result would be the worst of both worlds: *lower* short-term revenue and *no* control over pricing. The publishers recognized that, as a practical matter, this meant that the MFN Clause would force them to move Amazon to an agency

relationship. As Reidy put it, her company would need to move all its other ebook retailers to agency "unless we wanted to make even less money" in this growing market. *Apple*, 952 F. Supp. 2d at 666 (internal quotation marks omitted). This situation also gave each of the publishers a stake in Apple's quest to have a critical mass of publishers join the iBookstore because, "[w]hile no one Publisher could effect an industry-wide shift in prices or change the public's perception of a book's value, if they moved together they could." *Id.* at 665; *see also* J.A. 1981.

Apple understood this dynamic as well. As the district court found, "Apple did not change its thinking" when it replaced the explicit requirement that the publishers move other retailers to an agency model with the MFN. **[29]** Indeed, in the following weeks, Apple assiduously worked to make sure that the shift to agency occurred. *Apple*, 952 F. Supp. 2d at 663. But Apple also understood that, as Cue bluntly put it, "any decent MFN forces the model" away from wholesale and to agency. *Id.* (internal quotation marks omitted). Or as the district court found, "the MFN protected Apple from retail price competition as it punished a Publisher if it failed to impose agency terms on other e-tailers." *Id.* at 665.

Thus, the terms of the negotiation between Apple and the publishers became clear: Apple wanted quick and successful entry into the ebook market and to eliminate retail price competition with Amazon. In exchange, it offered the publishers an opportunity "to confront Amazon as one of an organized group … united in an effort to eradicate the $9.99 price point." *Id.* at 664. Both sides needed a critical mass of publishers to achieve their goals. The MFN played a pivotal role in this *quid pro quo* by "stiffen[ing] the spines of the [publishers] to ensure that they would demand new terms from Amazon," and protecting Apple from retail price competition. *Id.* at 665.

[30]

4. Final Negotiations

The proposed Contracts sparked intense negotiations as Cue's team raced to assemble enough publishers to announce the iBookstore by January 27. The publishers' first volley was to push back on Apple's price caps, which they recognized would become the "standard across the industry" for pricing.[5] J.A. 571. In a set of meetings between January 13 and 14, the majority of the Big Six expressed a general willingness to adopt an agency model, but refused to do so with the price limits Apple demanded. Cue responded by asking Jobs for permission to create a more lenient price cap system. Under this new regime, *New York Times* bestsellers could sell for $14.99 if the hardcover was listed above $30, and for $12.99 if listed below that price. As for new releases, a $12.99 cap would apply to hardcovers priced between $25 and $27.50; a $14.99 cap would apply to hardcovers selling for up to $30; and, if the hardcover sold for over $30, publishers could sell the ebook for between $16.99 and $19.99. Jobs responded that he could "live with" the pricing "as long as [the publishers] move Amazon to the agen[cy] model too." J.A. 499.

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[5] As one HarperCollins executive put it, the "upshot" of moving to the agency model and adopting price caps was that "Apple would control price and that price would be standard across the industry." *Apple*, 952 F. Supp. 2d at 670 (internal quotation marks omitted).

[31] Cue proposed this new pricing regime to the Big Six on January 16 and, with only 11 days remaining before the iPad launch, turned up the pressure. In each email conveying the new prices, Cue reminded the publishers that, if they did not agree to the iBookstore by the 27th, other companies, including Amazon and Barnes & Noble, would certainly build their own book store apps for the iPad. Correspondence from within the publishing companies also shows that Cue promoted the proposal as the "best chance for publishers to challenge the 9.99 price point," and emphasized that Apple would "not move forward with the store [unless] 5 of the 6 [major publishers] signed the agreement." J.A. 522-23. As Cue said at trial, he attempted to "assure [the publishers] that they weren't going to be alone, so that [he] would take the fear awa[y] of the Amazon retribution that they were all afraid of." J.A. 2068 (internal quotation marks omitted). "The Apple team reminded the Publishers," as the district court found, "that this was a rare opportunity for them to achieve control over pricing." *Apple*, 952 F. Supp. 2d at 664.

By January 22, two publishers—Simon & Schuster and Hachette—had verbally committed to join the iBookstore, while a third, Penguin, had agreed to Apple's terms in principle. As for the others, Cue was frustrated that they kept **[32]** "chickening out" because of the "dramatic business change" that Apple was proposing. J.A. 547. To make matters worse, "[p]ress reports on January 18 and 19 alerted the publishing world and Amazon to the Publishers' negotiations with Apple," *Apple*, 952 F. Supp. 2d at 670-71, and Amazon learned from Random House that it was facing "pressure from other publishers … to move to [the] agency model because Apple had made it clear that unless all of the Big Six participated, they wouldn't bother with building a bookstore," J.A. 1520. Representatives from Amazon descended on New York for a set of long scheduled meetings with the publishers. As the district court found, "[i]n separate conversations on January 20 and over the next few days, the Publisher Defendants all told Amazon that they wanted to change to an agency distribution model with Amazon." *Apple*, 952 F. Supp. 2d at 672.

Macmillan, however, presented an issue for Apple. The district court found that at a January 20 lunch between John Sargent and Amazon, Sargent "announced that Macmillan was planning to offer Amazon the option to choose either an agency [or wholesale] model." *Id.* But at dinner with Cue that night, according to the district court, Cue made sure that Sargent understood the consequences of the MFN, explaining "that Macmillan had no choice but to move **[33]** Amazon to an agency model if it wanted to sign an agency agreement with Apple."[6] *Id.* The next day, Sargent emailed Cue to express his continued reservations about switching Macmillan's other retailers to an agency relationship.

With the iPad launch fast approaching, Cue enlisted the help of others. Cue had received an email from Simon & Schuster's Carolyn Reidy, who had already verbally committed to Apple's terms and whom Cue would later call the "real leader of the book industry," moments after hearing from Sargent. J.A. 621. Cue then spoke with Reidy for twenty minutes before

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[6] Although Cue denied discussing the MFN that night, the district court found this testimony not credible in light of Cue's deposition testimony and his contemporaneous email to Jobs that Sargent had "legal concerns over the price matching." *Apple*, 952 F. Supp. 2d at 672 n.38 (internal quotation marks omitted). This determination was not clearly erroneous.

reaching out to Brian Murray, who, as the district court found, "was fully supportive of the requirement that all e-tailers be moved to an agency model." *Apple*, 952 F. Supp. 2d at 673 n.39. After the discussions, Cue asked Sargent to speak with both Reidy and Murray. Sargent complied, and "spoke to both Murray and Reidy by telephone for eight and fifteen minutes, respectively." *Id.* at 673. Minutes later, Sargent called the Amazon representative to inform him that Macmillan planned to sign an agreement that "required" the company to conduct business with **[34]** Amazon through an agency model. *Id.* By January 23, Macmillan had verbally agreed to join the iBookstore.

Cue followed a similar strategy with Penguin. While Penguin's CEO David Shanks agreed to Apple's terms on January 22, he informed Cue that he would join the iBookstore only if four other publishers agreed to participate. By January 25, Apple had signatures from three publishers but Penguin was still noncommittal. Cue called Shanks, and the two spoke for twenty minutes. "Less than an hour [later], Shanks called Reidy to discuss Penguin's status in its negotiations with Apple." *Id.* at 675. Penguin signed the Contract that afternoon.

HarperCollins was the fifth, and final, publisher to agree in principle to Apple's proposal. Murray, its CEO, "remained unhappy over the size of Apple's commission and the existence of price caps." *Id.* at 673 n.39. Unable to negotiate successfully with Murray, Cue asked Jobs to contact James Murdoch, the CEO of the publisher's parent company, and "tell him we have 3 signed so there is no leap of faith here." *Id.* at 675 (internal quotation marks omitted). After a series of emails, Jobs summarized Apple's position to Murdoch:

> [W]e simply don't think the ebook market can be successful with pricing higher than $12.99 or $14.99. Heck, Amazon is selling these books at $9.99, and who knows, maybe they are right and we will fail even at $12.99. But we're willing to try at the prices we've **[35]** proposed.... As I see it, [HarperCollins] has the following choices: (1) Throw in with [A]pple and see if we can all make a go of this to create a real mainstream ebooks market at $12.99 and $14.99. (2) Keep going with Amazon at $9.99. You will make a bit more money in the short term, but in the medium term Amazon will tell you they will be paying you 70% of $9.99. They have shareholders too. (3) Hold back your books from Amazon. Without a way for customers to buy your ebooks, they will steal them.

Id. at 677. Cue also emailed Murray to inform him that four other publishers had signed their agreements. Murray then called executives at both Hachette and Macmillan before agreeing to Apple's terms.

As the district court found, during the period in January during which Apple concluded its agreements with the Publisher Defendants, "Apple kept the Publisher Defendants apprised about who was in and how many were on board."[7] *Id.* at 673. The Publisher Defendants also kept in close communication. As the district court noted, "[i]n the critical negotiation period, over the three days between January 19 and 21, Mur-

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[7] Indeed, on the morning of January 21, Apple's initial deadline for the publishers to commit to agency, Simon & Schuster's Reidy emailed Cue to get "an update on your progress in herding us cats." J.A. 543.

ray, Reidy, Shanks, Young, and Sargeant called one another 34 times, with 27 calls exchanged on January 21 alone." *Id.* at 674.

[36] By the January 27 iPad launch, five of the Big Six—Hachette, HarperCollins, Macmillan, Penguin, and Simon & Schuster—had agreed to participate in the iBookstore. The lone holdout, Random House, did not join because its executives believed it would fare better under a wholesale pricing model and were unwilling to make a complete switch to agency pricing. Steve Jobs announced the iBookstore as part of his presentation introducing the iPad. When asked after the presentation why someone should purchase an ebook from Apple for $14.99 as opposed to $9.99 with Amazon or Barnes & Noble, Jobs confidently replied, "[t]hat won't be the case … the price will be the same.… [P]ublishers will actually withhold their [e]books from Amazon … because they are not happy with the price."[8] A day later, Jobs told his biographer the publishers' position with Amazon: "[y]ou're going to sign an agency contract or we're not going to give you the books." J.A. 891 (internal quotation marks omitted).

[37]

E. Negotiations with Amazon

Jobs's boast proved to be prophetic. While the Publisher Defendants were signing Apple's Contracts, they were also informing Amazon that they planned on changing the terms of their agreements with it to an agency model. However, their move against Amazon

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[8] On January 29, Simon & Schuster's general counsel wrote to Reidy that she "[could not] believe that Jobs made [this] statement," which she considered "[i]ncredibly stupid." J.A. 638.

began in earnest on January 28, the day after the iPad launch. That afternoon, John Sargent flew to Seattle to deliver an ultimatum on behalf of Macmillan: that Amazon would switch its ebook sales agreement with Macmillan to an agency model or suffer a seven-month delay in its receipt of Macmillan's new releases.[9] Amazon responded by removing the option to purchase Macmillan's print and ebook titles from its website.

Sargent, as the district court found, had informed Cue of his intention to confront Amazon before ever leaving for Seattle.[10] *Apple*, 952 F. Supp. 2d at 678. On his return, he emailed Cue to inform him about Amazon's decision to remove [38] Macmillan ebooks from Kindle, adding a note to say that he wanted to "make sure you are in the loop." J.A. 640. Sargent also wrote a public letter to Macmillan's authors and agents, describing the Amazon negotiations. Hachette's Arnaud Nourry emailed the CEO of Macmillan's parent company to express his "personal support" for Macmillan's actions and to "ensure [him] that [he was] not going to find [his] company alone in the battle." J.A. 643. A

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[9] As the district court found, "[s]even months was no random period—it was the number of months for which titles were designated New Release titles under the Apple Agreement and restrained by the Apple price caps and MFN." *Apple*, 952 F. Supp. 2d at 679.

[10] At trial, Cue claimed he had no advance knowledge of Sargent's plan to go to Seattle, but the district court found this testimony to be incredible. Sargent had emailed Cue about his trip days before the meeting took place. Moreover, on January 28, the day of the meeting, Jobs told his biographer that the Publisher Defendants "went to Amazon and said, 'You're going to sign an agency contract or we're not going to give you the books.'" *Apple*, 952 F. Supp. 2d at 678 n.47. The district court's assessment of Cue's credibility was not clearly erroneous.

Penguin executive wrote to express similar support for Macmillan's position.

The district court found that while Amazon was "opposed to adoption of the agency model and did not want to cede pricing authority to the Publishers," it knew that it could not prevail in this position against five of the Big Six. *Apple*, 952 F. Supp. 2d at 671, 680. When Amazon told Macmillan that it would be willing to negotiate agency terms, Sargent sent Cue an email titled "URGENT!!" that read: "Hi Eddy, I am gonna need to figure out our final agency terms of sale tonight. Can you call me please?" J.A. 642. Cue and Sargent spoke that night and, while Cue denied at trial that the conversation concerned Macmillan's negotiations with Amazon, the district court found that "his denial was not [39] credible."[11] *Apple*, 952 F. Supp. 2d at 681 n.52. By February 5, Amazon had agreed to agency terms with Macmillan.

The other publishers who had joined the iBookstore quickly followed Macmillan's lead. On February 11, Reidy wrote to the head of CBS that Simon & Schuster was beginning agency negotiations with Amazon. She informed him that she was trying to "delay" negotiations because it was "imperative … that the other publishers with whom Apple has announced deals push for resolution on their term changes" at the same time, "thus not leaving us out there alone." J.A. 701. Each of the Publisher Defendants then informed Amazon that they were under tight deadlines to negotiate new agency agreements, and kept one another in-

[11] As the district court noted, Macmillan had executed its Contract with Apple a week earlier, so that "the only final agency terms still under discussion were with Amazon." *Apple*, 952 F. Supp. 2d at 681 n.52.

formed about the details of their negotiations. As David Naggar, one of Amazon's negotiators, testified, whenever Amazon "would make a concession on an important deal point," it would "come back to us from another publisher asking for the same thing or proposing similar language." J.A. 1491.

Once again, Apple closely monitored the negotiations with Amazon. The Publisher Defendants would inform Cue when they had completed agency agreements, and his team monitored price changes on the Kindle. When **[40]** Penguin languished behind the others, Cue informed Jobs that Apple was "changing a bunch of Penguin titles to 9.99" in the iBookstore "because they didn't get their Amazon deal done." *Apple*, 952 F. Supp. 2d at 682 (internal quotation marks omitted). By March 2010, Macmillan, HarperCollins, Hachette, and Simon & Schuster had completed agency agreements with Amazon. When Penguin completed its deal in June, the company's executive proudly announced to Cue that "[t]he playing field is now level." *Id.* (internal quotation marks omitted).[12]

F. Effect on Ebook Prices

As Apple and the Publisher Defendants expected, the iBookstore price caps quickly became the benchmark for ebook versions of new releases and *New York Times* bestsellers. In the five months following the launch of the iBookstore, the publishers who joined the marketplace and switched Amazon to an agency model priced 85.7% of new releases on Kindle and 92.1% of

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[12] Eventually, the Publisher Defendants negotiated agency agreements with Barnes & Noble, and later Google. Random House also adopted the agency model, and joined the iBookstore, in early 2011.

new releases on the iBookstore at, or just below, the price caps. *Apple*, 952 F. Supp. 2d at 682. Prices for *New York Times* bestsellers took a similar leap as publishers began to sell **[41]** 96.8% of their bestsellers on Kindle and 99.4% of their bestsellers on the iBookstore at, or just below, the Apple price caps. *Id.* During that same time period, Random House, which had not switched to an agency model, saw virtually no change in the prices for its new releases or *New York Times* bestsellers.

The Apple price caps also had a ripple effect on the rest of the Publisher Defendants' catalogues. Recognizing that Apple's price caps were tied to the price of hardcover books, many of these publishers increased the prices of their newly released *hardcover* books to shift the ebook version into a higher price category. *Id.* at 683. Furthermore, because the Publisher Defendants who switched to the agency model expected to make less money per sale than under the wholesale model, they also increased the prices on their ebooks that were *not* new releases or bestsellers to make up for the expected loss of revenue.[13] Based on data from February 2010—just before the Publisher Defendants switched Amazon to agency pricing—to February 2011, an expert retained by the Justice Department observed that the weighted average price of the Publisher Defendants' new releases increased by 24.2%, while bestsellers increased by **[42]** 40.4%, and other ebooks increased by 27.5%, for a total weighted average ebook

[13] The five Publisher Defendants accounted for 48.8% of all retail trade ebook sales in the United States during the first quarter of 2010.

price increase of 23.9%.[14] Indeed, even Apple's expert agreed, noting that, over a two-year period, the Publisher Defendants increased their average prices for hardcovers, new releases, and other ebooks.

Increasing prices reduced demand for the Publisher Defendants' ebooks. According to one of Plaintiffs' experts, the publishers who switched to agency sold 77,307 fewer ebooks over a two-week period after the switch to agency than in a comparable two-week period before the switch, which amounted to selling 12.9% fewer units. *Id.* at 684. Another expert relied on data from Random House to estimate how many ebooks the Publisher Defendants who switched Amazon to agency would have sold had they stayed with the wholesale model, and concluded that the agency switch and price increases led to 14.5% fewer sales. *Id.*

Significantly, these changes took place against the backdrop of a rapidly changing ebook market. Amazon introduced the Kindle in November 2007, just over two years before Apple launched the iPad in January 2010. During that short period, Apple estimated that the market grew from $70 million in ebook **[43]** sales in 2007 to $280 million in 2009, and the company projected those figures to grow significantly in following years. Apple's expert witnesses argued that overall ebook sales continued to grow in the two years after the creation of the iBookstore and that the average ebook price fell during those years. But as Plaintiffs' experts pointed out, the ebook market had been expanding rapidly even before Apple's entry and average prices had been falling as lower-end publishers entered the market and larger

[14] A weighted average price controls for the fact that different ebooks sell in different quantities by dividing the total price that consumers paid for ebooks by the total number of ebooks sold.

numbers of old books became available in digital form. "Apple's experts did not present any analysis that attempted to control for the many changes that the e-book market was experiencing during these early years of its growth," *Apple*, 952 F. Supp. 2d at 685, nor did they estimate how the market would have grown *but for* Apple's agreement with the Publisher Defendants to switch to an agency model and raise prices. To the contrary, the undisputed fact that the Publisher Defendants raised prices on their ebooks, which accounted for roughly 50% of the trade ebook market in the first quarter of 2010, necessitated "a finding that the actions taken by Apple and the Publisher Defendants led to an increase in the price of e-books." *Id.*

Finally, in response to the dissent's claim that Apple's conduct "deconcentrat[ed] … the e-book retail market" and thus was "pro-competitive," **[44]** Dissenting Op. at 31, it is worth noting that the district court's economic analysis and the parties' submissions at trial focused entirely on the price and sales figures for trade ebooks. This is because both parties agreed that the relevant market in this case is "the trade e-books market, not the e-reader market or the 'e-books system' market." *United States v. Apple, Inc.*, 889 F. Supp. 2d 623, 642 (S.D.N.Y. 2012); *Apple*, 952 F. Supp. 2d at 694 n.60. The district court did not analyze the state of competition between ebook *retailers* or determine that Amazon's pricing policy acted, as the dissent accuses, as a "barrier[] to entry" for other potential retailers. Dissenting Op. at 24, 30.

II. Procedural History

On April 11, 2012, Plaintiffs filed a pair of civil antitrust actions in the United States District Court for the Southern District of New York. The complaints alleged that Apple and the Publisher Defendants—Hachette, HarperCollins, Macmillan, Penguin, and Simon & Schuster—conspired to raise, fix, and stabilize the retail price for newly released and bestselling trade ebooks in violation of § 1 of the Sherman Act and various state laws. The litigation then proceeded along two separate trajectories, one for the Publisher Defendants and the other for Apple.

[45]

A. Publisher Defendants

Hachette, HarperCollins, and Simon & Schuster agreed to settle with DOJ by signing consent decrees on the same day that the Justice Department filed its complaint. Pursuant to the Tunney Act, 15 U.S.C. § 16 *et seq.*, "at least 60 days prior to the effective date" of a consent judgment, the United States must file a "competitive impact statement," which includes, *inter alia*, "the nature and purpose of the proceeding," "a description of the practices or events giving rise to the alleged violation of the antitrust laws," and an explanation of the relief obtained by the consent judgment "and the anticipated effects on competition of such relief." *Id.* § 16(b). In compliance with these requirements, DOJ issued a competitive impact statement that outlined the remedies it planned to impose on Hachette, HarperCollins, and Simon & Schuster. Two of those proposed remedies required that, for two years, the three publishers "not restrict, limit, or impede an E-book Retailer's ability to set, alter, or reduce the Retail Price of any E-book or to offer price discounts or any other form of promotions," and that they not "enter into any agreement" with retailers that limit such practices. J.A. 1126-27.

[46] After the 60-day comment period, the Justice Department moved in the district court for a decision

that "the entry of the judgment is in the public interest," 15 U.S.C. § 16(e), and for approval of the consent decree. In defense of the two-year limitations provisions, DOJ explained that the Publisher Defendants had used retail price restrictions to "effectuat[e] the conspiracy" and that two years was sufficient to "allow movement in the marketplace away from collusive conditions" without "alter[ing] the ultimate development of the competitive landscape in the still-evolving e-books industry." J.A. 1054-55. On September 5, 2012, the district court approved the consent decree and found the two-year ban on retail-price restrictions "wholly appropriate given the Settling Defendants' alleged abuse of such provisions … , the Government's recognition that such terms are not intrinsically unlawful, and the nascent state of competition in the ebooks industry." J.A. 1088.

The remaining Publisher Defendants, Penguin and Macmillan, settled in quick succession. On December 18, 2012, Penguin agreed to a consent decree with essentially the same terms that Hachette, HarperCollins, and Simon & Schuster received. A few months later, in February 2013, Macmillan also agreed to settle. The terms of Macmillan's consent decree contained slight **[47]** modifications. Rather than delaying the prohibition on retail discounts until the court approved the decree, DOJ required Macmillan to begin compliance within three days of signing the decree. In exchange, the Justice Department agreed to back-date the beginning of the limitations period to December 18, 2012 and to reduce its length from two years to 23 months, explaining that "[c]onsumers are better served by bringing more immediate retail price competition to the market" and that a "23-month cooling-off period is sufficient" to restore competition. J.A. 1162-63. The district court approved Penguin's consent decree on May 17, 2013, and Macmillan's on August 12, 2013.

B. Apple

Unlike the Publisher Defendants, Apple opted to take the case to trial. Fact and expert discovery concluded on March 22, 2013 and, after filing pretrial motions, the parties agreed to a bench trial on Apple's liability and injunctive relief, to be followed by a separate trial on damages on the state claims if the states prevailed.

On July 10, 2013, after conducting a three-week bench trial, the district court concluded that Apple had violated § 1 of the Sherman Act and various state antitrust laws. In brief, the court found that Apple "orchestrat[ed]" a conspiracy [48] among the Publisher Defendants to "eliminate retail price competition [in the ebook market] in order to raise the retail prices of e-books." *Apple*, 952 F. Supp. 2d at 697. Because this conspiracy consisted of a group of competitors—the Publisher Defendants—assembled by Apple to increase prices, it constituted a "horizontal price-fixing conspiracy" and was a *per se* violation of the Sherman Act. *Id.* at 694. It concluded, moreover, that even if the agreement to raise prices and eliminate retail price competition were analyzed under the rule of reason, it would still constitute an unreasonable restraint of trade in violation of § 1. *Id.* In the district court's view, Plaintiffs' experts persuasively demonstrated that the agreement facilitated an "across-the board price increase in e-books sold by the Publisher Defendants" and a corresponding drop in sales. *Id.* Apple, on the other hand, failed to show that "the execution of the Agreements," as opposed to the launch of the iPad and "evolution of digital publishing more generally" (which were independent of the Agreements), "had any procompetitive effects." *Id.*

After the district court issued its liability decision, the parties submitted briefing on injunctive relief. The court conducted a hearing on the issue and, on September 5, 2013, issued a final injunctive order against Apple and entered final **[49]** judgment. The injunctive order consists of four categories of relief: (1) "Prohibited Conduct," which prevents Apple from enforcing MFNs with ebook publishers, retaliating against publishers for signing agreements with other retailers, or agreeing with any of the Publisher Defendants to restrict, limit, or impede Apple's ability to set ebook retail prices; (2) "Required Conduct," which, among other things, forces Apple to modify its agency agreements with the Publisher Defendants and to treat ebook apps sold in the iTunes store like any other app sold there; (3) "Antitrust Compliance," which requires Apple to improve its internal system for preventing antitrust violations; and (4) "External Compliance Monitor[ing]," which allows the court to appoint an external monitor to ensure Apple's compliance with the injunctive order.

After the entry of the district court's injunctive order, Apple, Macmillan, and Simon & Schuster filed this appeal. The parties have not yet conducted a trial to assess the damages stemming from the state antitrust claims.

[50]

DISCUSSION

To hold a defendant liable for violating § 1 of the Sherman Act, a district court must find "a combination or some form of concerted action between at least two legally distinct economic entities" that "constituted an unreasonable restraint of trade." *Capital Imaging Assocs. v. Mohawk Valley Med. Assocs.*, 996 F.2d 537, 542 (2d Cir. 1993); *see* 15 U.S.C. § 1. On appeal, Apple challenges numerous aspects of the district court's § 1 analysis and also contends that the injunctive order that the district court imposed on the company is unlawful. Macmillan and Simon & Schuster have joined Apple's challenge to the injunction, arguing that it impermissibly interferes with their consent decrees and is barred by the doctrine of judicial estoppel. We conclude that the district court's liability determination was sound and its injunctive order lawful. We therefore affirm the judgment of the district court.

I. Standard of Review

Following a bench trial, this Court reviews the "district court's findings of fact for clear error" and its "conclusions of law and mixed questions *de novo*." *Connors v. Conn. Gen. Life Ins. Co.*, 272 F.3d 127, 135 (2d Cir. 2001); *see* Fed. R. Civ. P. 52(a). The district court's evidentiary rulings and its fashioning of equitable **[51]** relief are reviewed for abuse of discretion. *See Zerega Ave. Realty Corp. v. Hornbeck Offshore Transp., LLC*, 571 F.3d 206, 212-13 (2d Cir. 2009) (evidentiary rulings); *Abrahamson v. Bd. of Educ. Of the Wappingers Falls Cent. Sch. Dist.*, 374 F.3d 66, 76 (2d Cir. 2004) (equitable relief).

II. Apple's Liability Under § 1

This appeal requires us to address the important distinction between "horizontal" agreements to set prices, which involve coordination "between competitors at the same level of [a] market structure," and "vertical" agreements on pricing, which are created between parties "at different levels of [a] market structure." *Anderson News, L.L.C. v. Am. Media, Inc.*, 680

F.3d 162, 182 (2d Cir. 2012) (internal quotation marks omitted). Under § 1 of the Sherman Act, the former are, with limited exceptions, *per se* unlawful, while the latter are unlawful only if an assessment of market effects, known as a rule-of-reason analysis, reveals that they unreasonably restrain trade. *See Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 893 (2007).

Although this distinction is sharp in theory, determining the orientation of an agreement can be difficult as a matter of fact and turns on more than simply identifying whether the participants are at the same level of the market structure. **[52]** For instance, courts have long recognized the existence of "hub-and-spoke" conspiracies in which an entity at one level of the market structure, the "hub," coordinates an agreement among competitors at a different level, the "spokes." *Howard Hess Dental Labs. Inc. v. Dentsply Int'l, Inc.*, 602 F.3d 237, 255 (3d Cir. 2010); *see also Toys "R" Us, Inc. v. FTC*, 221 F.3d 928, 932-34 (7th Cir. 2000). These arrangements consist of *both* vertical agreements between the hub and each spoke and a horizontal agreement among the spokes "to adhere to the [hub's] terms," often because the spokes "would not have gone along with [the vertical agreements] except on the understanding that the other [spokes] were agreeing to the same thing." VI Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 1402c (3d ed. 2010) (citing *PepsiCo, Inc. v. Coca-Cola Co.*, 315 F.3d 101 (2d Cir. 2002)); *see also* Am. Bar Ass'n, *Antitrust Law Developments* 24-26 (6th ed. 2007); XII Areeda & Hovenkamp, *supra*, ¶ 2004c.[15]

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[15] In this sense, the "hub-and-spoke" metaphor is somewhat inaccurate—the plaintiff must also prove the existence of a "rim"

Apple characterizes its Contracts with the Publisher Defendants as a series of parallel but independent vertical agreements, a characterization that forms the basis for its two primary arguments against the district court's decision. First, [53] Apple argues that the district court impermissibly inferred its involvement in a horizontal price-fixing conspiracy from the Contracts themselves. Because (in Apple's view) the Contracts were vertical, lawful, and in Apple's independent economic interest, the mere fact that Apple agreed to the same terms with multiple publishers cannot establish that Apple consciously organized a conspiracy among the Publisher Defendants to raise consumer-facing ebook prices—even if the *effect* of its Contracts was to raise those prices. Second, Apple argues that, even if it did orchestrate a horizontal price-fixing conspiracy, its conduct should not be subject to *per se* condemnation. According to Apple, proper application of the rule of reason reveals that its conduct was not unlawful.

For the reasons set forth below, we reject these arguments. On this record, the district court did not err in determining that Apple orchestrated an agreement with and among the Publisher Defendants, in characterizing this agreement as a horizontal price fixing-conspiracy, or in holding that the conspiracy unreasonably restrained trade in violation of § 1 of the Sherman Act.

A. The Conspiracy with the Publisher Defendants

Section 1 of the Sherman Act bans restraints on trade "effected by a contract, combination, or conspira-

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to the wheel in the form of an agreement among the horizontal competitors. *See Dickson v. Microsoft Corp.*, 309 F.3d 193, 203-04 (4th Cir. 2002).

cy." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 553 **[54]** (2007) (internal quotation marks omitted). The first "crucial question in a Section 1 case is therefore whether the challenged conduct 'stem[s] from independent decision or from an agreement, tacit or express.'" *Starr v. Sony BMG Music Entm't*, 592 F.3d 314, 321 (2d Cir. 2010) (alteration in original) (quoting *Theatre Enters., Inc. v. Paramount Film Distrib. Corp.*, 346 U.S. 537, 540 (1954)).

Identifying the existence and nature of a conspiracy requires determining whether the evidence "reasonably tends to prove that the [defendant] and others had a conscious commitment to a common scheme designed to achieve an unlawful objective." *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 (1984) (internal quotation marks omitted). Parallel action is not, by itself, sufficient to prove the existence of a conspiracy; such behavior could be the result of "coincidence, independent responses to common stimuli, or mere interdependence unaided by an advance understanding among the parties." *Twombly*, 550 U.S. at 556 n.4 (internal quotation marks omitted). Indeed, parallel behavior that does not result from an agreement is not unlawful even if it is anticompetitive. *See In re Text Messaging Antitrust Litig.*, 782 F.3d 867, 873-79 (7th Cir. 2015); *In re Flat Glass Antitrust Litig.*, 385 F.3d 350, 360-61 (3d Cir. 2004). Accordingly, to prove an antitrust conspiracy, "a plaintiff must show the **[55]** existence of additional circumstances, often referred to as 'plus' factors, which, when viewed in conjunction with the parallel acts, can serve to allow a fact finder to infer a conspiracy." *Apex Oil Co. v. DiMauro*, 822 F.2d 246, 253 (2d Cir. 1987).

These additional circumstances can, of course, consist of "direct evidence that the defendants entered into an agreement" like "a recorded phone call in which two competitors agreed to fix prices." *Mayor & City Council of Baltimore, Md. v. Citigroup, Inc.*, 709 F.3d 129, 136 (2d Cir. 2013). But plaintiffs may also "present circumstantial facts supporting the *inference* that a conspiracy existed." *Id.* Circumstances that may raise an inference of conspiracy include "a common motive to conspire, evidence that shows that the parallel acts were against the apparent individual economic self-interest of the alleged conspirators, and evidence of a high level of interfirm communications." *Id.* (internal quotation marks omitted). Parallel conduct alone may support an inference of conspiracy, moreover, if it consists of "complex and historically unprecedented changes in pricing structure made at the very same time by multiple competitors, and made for no other discernible reason." *Id.* at 137 (internal quotation marks omitted).

[56] Because of the risk of condemning parallel conduct that results from independent action and not from an actual unlawful agreement, the Supreme Court has cautioned against drawing an inference of conspiracy from evidence that is equally consistent with independent conduct as with illegal conspiracy—or, as the Court has called it, "ambiguous" evidence. *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 597 n.21 (1986). Thus, a finding of conspiracy requires "evidence that tends to exclude the possibility" that the defendant was "acting independently." *Monsanto*, 465 U.S. at 764. This requirement, however, "[does] not mean that the plaintiff must disprove all nonconspiratorial explanations for the defendants' conduct"; rather, the evidence need only be sufficient "to allow a reasonable fact finder to infer that the conspiratorial explanation is more likely than not." *In re Publ'n Paper Anti-*

trust Litig., 690 F.3d 51, 63 (2d Cir. 2012) (quoting Phillip E. Areeda & Herbert Hovenkamp, *Fundamentals of Antitrust Law* § 14.03(b), at 14-25 (4th ed. 2011)); *accord Matsushita*, 475 U.S. at 588 (requiring that "the inference of conspiracy is reasonable in light of the competing inferences of independent action"); *In re High Fructose Corn Syrup Antitrust Litig.*, 295 F.3d 651, 655-56 (7th Cir. 2002).

[57] Apple portrays its Contracts with the Publisher Defendants as, at worst, "unwittingly facilitat[ing]" their joint conduct. Apple Br. at 23. All Apple did, it claims, was attempt to enter the market on profitable terms by offering contractual provisions—an agency model, the MFN Clause, and tiered price caps—which ensured the company a small profit on each ebook sale and insulated it from retail price competition. This had the *effect* of raising prices because it created an incentive for the Publisher Defendants to demand that Amazon adopt an agency model and to seize control over consumer-facing ebook prices industry-wide. But although Apple knew that its contractual terms would entice the Publisher Defendants (who wanted to do away with Amazon's $9.99 pricing) to seek control over prices from Amazon and other ebook retailers, Apple's success in capitalizing on the Publisher Defendants' preexisting incentives, it contends, does not suggest that it joined a *conspiracy* among the Publisher Defendants to raise prices. In sum, Apple's basic argument is that because its Contracts with the Publisher Defendants were fully consistent with its independent business interests, those agreements provide only "ambiguous" evidence of a § 1 conspiracy, and the district court therefore erred under *Matsushita and Monsanto* in inferring such a conspiracy.

[58] We disagree. At the start, Apple's benign portrayal of its Contracts with the Publisher Defendants is not persuasive—not because those Contracts themselves were independently unlawful, but because, in context, they provide strong evidence that Apple consciously orchestrated a conspiracy among the Publisher Defendants. As explained below, and as the district court concluded, Apple understood that its proposed Contracts were attractive to the Publisher Defendants *only* if they collectively shifted their relationships with Amazon to an agency model—which Apple knew would result in higher consumer-facing ebook prices. In addition to these Contracts, moreover, ample additional 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. The district court did not err in concluding that Apple was more than an innocent bystander.

Apple offered each Big Six publisher a proposed Contract that would be attractive only if the publishers acted collectively. 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 [59] to stomach this loss because the model allowed them to sell new releases and bestsellers for more than $9.99. Because of the MFN Clause, however, each new release and bestseller sold in the iBookstore would cost only $9.99 as long as Amazon continued to sell ebooks at that price. So in order to receive the perceived benefit of Apple's proposed Contracts, the Publisher Defendants had to switch *Amazon* to an agency model as well—something no individual publisher had sufficient leverage to do on its own. Thus, each Publisher Defendant would be able to accomplish the shift to agency—and therefore have an incentive to sign Apple's proposed Contracts—*only* if it acted in tandem with its competitors. *See Starr*, 592 F.3d at 324; *Flat Glass*, 385 F.3d at 360-61; *see also* J.A. 1974 (noting that the agreements would "not fix the publishers' problems" if they could not move Amazon to an agency model). By the very act of signing a Contract with Apple containing an MFN Clause, then, each of the Publisher Defendants signaled a clear commitment to move against Amazon, thereby facilitating their collective action. As the district court explained, the MFNs "stiffened the spines" of the Publisher Defendants. *Apple*, 952 F. Supp. 2d at 665.

As a sophisticated negotiator, Apple was fully aware that its proposed Contracts would entice a critical mass of publishers only if these publishers **[60]** perceived an opportunity collectively to shift Amazon to agency.[16] In fact, this was the very purpose of the MFN, which Apple's Saul devised as an elegant alternative to a provision that would have explicitly *required* the publishers to adopt an agency model with other retailers. As Cue put it, the MFN "force[d] the model" from wholesale to agency. J.A. 865. Indeed, the MFN's capacity for forcing collective action by the pub-

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[16] Apple's argument on appeal that it did not have sufficient market power to coordinate the Publisher Defendants is beside the point. Market power may afford one means by which a company can coerce others to comply with its wishes, but brute force is not the only way to foster an agreement. Here, both Apple and the Publisher Defendants understood that Apple was in a position to "solve" the publishers' "Amazon problem" by helping them eliminate what they saw as a mortal threat to their businesses—namely, the $9.99 price point.

lishers 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—the same, Jobs said, because the publishers would make Amazon "sign … agency contract[s]" by threatening to withhold their ebooks. J.A. 891. Apple was also fully aware that once the Publisher Defendants seized control over consumer-facing ebook prices, those prices would rise. It knew from the outset that the publishers hated Amazon's $9.99 price point, and it put price caps in its agreements because it specifically anticipated that once the publishers gained control over prices, they **[61]** would push them higher than $9.99, higher than Apple itself deemed "realistic." *Apple*, 952 F. Supp. 2d at 692 (internal quotation marks omitted).

On appeal, Apple nonetheless defends the Contracts that it proposed to the publishers as an "aikido move" that shrewdly leveraged market conditions to its own advantage. Apple Br. at 17. "[A]ikido move" or not, the attractiveness of Apple's offer to the Publisher Defendants hinged on whether it could successfully help organize them to force Amazon to an agency model and then to use their newfound collective control to raise ebook prices. The Supreme Court has defined an agreement for Sherman Act § 1 purposes as "a conscious commitment to a common scheme designed to achieve an unlawful objective." *Monsanto*, 465 U.S. at 764 (internal quotation marks omitted). Plainly, this use of the promise of higher prices as a bargaining chip to induce the Publisher Defendants to participate in the iBookstore constituted a conscious commitment to the goal of raising ebook prices. "Antitrust law has never required identical *motives* among conspirators" when their independent reasons for joining together lead to collusive action. *Spectators' Commc'n Network Inc. v. Colonial Country Club*, 253 F.3d 215, 220 (5th Cir. 2001) (emphasis added). Put differently, "independent reasons" can also be "interdependent," and the fact that Apple's conduct was in **[62]** its own economic interest in no way undermines the inference that it entered an agreement to raise ebook prices. VI Areeda & Hovenkamp, *supra*, ¶ 1413a (internal quotation marks omitted).

Nor was the Publisher Defendants' joint action against Amazon a result of parallel decisionmaking. As we have explained, conduct resulting solely from competitors' independent business decisions—and not from any "agreement"—is not unlawful under § 1 of the Sherman Act, even if it is anticompetitive. *See Text Messaging*, 782 F.3d at 873-79. But to generate a permissible inference of agreement, a plaintiff need only present sufficient evidence that such agreement was more likely than not. On this record, the district court had ample basis to conclude that it was not equally likely that the near-simultaneous signing of Apple's Contracts by multiple publishers—which led to all of the Publisher Defendants moving against Amazon—resulted from the parties' independent decisions, as opposed to a "meeting of [the] minds." *Monsanto*, 465 U.S. at 765; *see Toys "R" Us*, 221 F.3d at 935-36 (holding that exclusive-dealing agreements between a retailer and manufacturers that were contrary to the manufacturers' individual self-interest but consistent with their collective interest supported the inference of a horizontal conspiracy in which the retailer participated); VI Areeda & **[63]** Hovenkamp, *supra*, ¶ 1425a, d ("[A] conspiracy may be inferred if a defendant's action would have been contrary to its self-interest in the absence of advance agreement." *Id.* ¶ 1425a). That the

Publisher Defendants were in constant communication regarding their negotiations with both Apple and Amazon can hardly be disputed. Indeed, Apple never seriously argues that the Publisher Defendants were not acting in concert.

Even so, Apple claims, it cannot have organized the conspiracy among the Publisher Defendants if it merely "unwittingly facilitated [their] joint conduct." Apple Br. at 23. But this argument founders—and dramatically so—on the factual findings of the district court. As the district court explained, Apple's Contracts with the publishers "must be considered in the context of the entire record." *Apple*, 952 F. Supp. 2d at 699. Even if Apple was unaware of the extent of the Publisher Defendants' coordination when it first approached them,[17] its **[64]** subsequent communications with them as negotiations progressed show that Apple consciously played a key role in organizing their express collusion. From the outset, Cue told the publishers that Apple would launch its iBookstore only if a sufficient number of them agreed to participate and that each publisher would receive

[17] Apple endeavors to draw the district court's factfinding into doubt by asserting, erroneously, that the "bedrock of the court's entire decision" hinges on its supposed determination that Apple, knowing that the publishers had been coordinating beforehand, joined a preexisting conspiracy to raise prices at its initial meetings with the Publisher Defendants—a proposition that, it says, is unsupported by the record. The district court, however, did *not* find that Apple joined an ongoing conspiracy in late 2009, but merely observed that Apple went into its initial meetings with the understanding that the Publisher Defendants disliked, and were trying to fight, Amazon's $9.99 pricing, and so would be receptive to the news that Apple was open to higher prices. *See Apple*, 952 F. Supp. 2d at 703. *These* findings were amply supported and help explain how the agreement among Apple and the Publisher Defendants thereafter emerged.

identical terms, assuring them that a critical mass of major publishers would be prepared to move against Amazon. Later on, Cue and his team kept the publishers updated about how many of their peers signed Apple's Contracts, and reminded them that it was offering "the best chance for publishers to challenge the 9.99 price point" before it became "cement[ed]" in "consumer expectations." J.A. 522. When time ran short, Apple coordinated phone calls between the publishers who had agreed and those who remained on the fence.[18] **[65]** As Cue said at trial, Apple endeavored to "assure [the publishers] that they weren't going to be alone, so that [Apple] would take the fear awa[y] of the Amazon retribution that they were all afraid of." J.A. 2068.

Apple's involvement in the conspiracy continued even past the signing of its agency agreements. Before Sargent flew to Seattle to meet with Amazon, he told Cue. Apple stayed abreast of the Publisher Defendants' progress as they set coordinated deadlines with Amazon and shared information with one another during negotiations. Apple's communications with the Publisher De-

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[18] Apple takes issue with the district court's conclusion that Apple was aware of, and facilitated, communication between the Publisher Defendants. But the district court found that Cue believed Reidy was a "leader" in the publishing industry and that, on at least two occasions toward the end of the negotiating period, Cue called a recalcitrant executive, who then spoke to Reidy before agreeing to Apple's terms. *See Apple*, 952 F. Supp. 2d at 659-60; J.A. 2019-20. Reidy herself adverted to Cue's role in "herding us cats." J.A. 543. Moreover, the publishing executives frequently denied having *any* conversations about Apple during this period, despite strong documentary and phone record evidence to the contrary. The district court found that these denials lacked credibility and "strongly support[ed] a finding of consciousness of guilt." *Apple*, 952 F. Supp. 2d at 693 n.59. This view of the facts is not clearly erroneous.

fendants thus went well beyond legitimately "exchang[ing] information" within "the normal course of business," *Monsanto*, 465 U.S. at 762-63 (internal quotation marks omitted), or "friendly banter among business partners," Apple Br. at 38; *see Monsanto*, 465 U.S. at 765-66 (concluding that message about getting "the market place in order" could lead to inference of conspiracy (internal quotation marks omitted)); *see also Starr*, 592 F.3d at 324; *Apex Oil*, 822 F.2d at 255-57.

Apple responds to this evidence—which the experienced judge who oversaw the trial characterized repeatedly as "overwhelming"—by explaining how each piece of evidence standing alone is "ambiguous" and therefore insufficient to support an inference of conspiracy. We are not persuaded. In **[66]** antitrust cases, "[t]he character and effect of a conspiracy are not to be judged by dismembering it and viewing its separate parts, but only by looking at it as a whole." *Cont'l Ore Co. v. Union Carbide & Carbon Corp.*, 370 U.S. 690, 699 (1962). Combined with the unmistakable purpose of the Contracts that Apple proposed to the publishers, and with the collective move against Amazon that inevitably followed the signing of those Contracts, the emails and phone records demonstrate that Apple *agreed* with the Publisher Defendants, within the meaning of the Sherman Act, to raise consumer-facing ebook prices by eliminating retail price competition. The district court did not err in rejecting Apple's argument that the evidence of its orchestration of the Publisher Defendants' conspiracy was "ambiguous."

Given the record and the district court's factual findings, we do not share Apple and its amici's concern that we will stifle productive enterprise by inferring an agreement among Apple and the Publisher Defendants on the basis of otherwise lawful contract terms, such as an agency model and MFNs. To begin with, it is well established that vertical agreements, lawful in the abstract, can in context "be useful evidence for a plaintiff attempting to prove the existence of a horizontal cartel," *Leegin*, 551 U.S. at 893, particularly where **[67]** multiple competitors sign vertical agreements that would be against their own interests were they acting independently, *see, e.g.*, *Interstate Circuit v. United States*, 306 U.S. 208, 222 (1939); *Toys "R" Us*, 221 F.3d at 935-36. The MFNs in Apple's Contracts created a set of economic incentives pursuant to which the Contracts were only attractive to the Publisher Defendants to the extent they acted collectively. That these contract terms had such an effect under the particular circumstances of this case—and therefore furnish part of the evidence of Apple's agreement with the Publisher Defendants—says nothing about their broader legality. It should be self-evident that our analysis is informed by the particular context in which Apple's contract terms were deployed. In any event, we are breaking no new ground in concluding that MFNs, though surely proper in many contexts, can be "misused to anticompetitive ends in some cases." *Blue Cross & Blue Shield United of Wis. v. Marshfield Clinic*, 65 F.3d 1406, 1415 (7th Cir. 1995); *see Starr*, 592 F.3d at 324 (finding MFN evidence of conspiracy). Under the right circumstances, an MFN can "facilitate anticompetitive horizontal coordination" by "reduc[ing] [a company's] incentive to deviate from a coordinated horizontal arrangement." Jonathan B. Baker, *Vertical Restraints with Horizontal Consequences: Competitive Effects of "Most-Favored-Customer" Clauses*, 64 **[68]** Antitrust L.J. 517, 520-21 (1996); *see also* Jonathan B. Baker & Judith A. Chevalier, *The Competitive Consequences of Most-Favored-Nation Provisions*, Antitrust, Spring 2013, at 20-26, *available at* http://digitalcommons.wcl.american.edu/cgi/viewcontent.cgi?article=1280&context=facsch_lawrev.[19]

In short, we have no difficulty on this record rejecting Apple's argument that the district court erred in concluding that Apple "conspir[ed] with the Publisher Defendants to eliminate retail price competition and to raise e-book prices." *Apple*, 952 F. Supp. 2d at 691. Having concluded that the district court correctly identified an agreement between Apple and the Publisher Defendants to raise consumer-facing ebook prices, we turn to Apple's and the dissent's arguments that this agreement did not violate § 1 of the Sherman Act.

[69]

B. Unreasonable Restraint of Trade

"Although the Sherman Act, by its terms, prohibits every agreement 'in restraint of trade,' [the Supreme] Court has long recognized that Congress intended to outlaw only unreasonable restraints." *State Oil Co. v.*

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[19] Nor does our holding remotely suggest that price caps are always unlawful, which they are not. *See State Oil Co. v. Khan*, 522 U.S. 3 (1997) (holding that vertical maximum price-fixing agreements should be analyzed under the rule of reason). Apple required price caps because it knew that once the Publisher Defendants moved on Amazon to seize control over ebook prices, they would raise them. Apple wanted to ensure that the Publisher Defendants set "realistic prices" that reflected the lower costs of producing ebooks. J.A. 359. The Publisher Defendants and Apple understood that these caps would become the "standard across the industry." J.A. 573. The price negotiations therefore reflected a common understanding that prices would rise, but a difference of opinion among the co-conspirators over *how high* they could reasonably go. *See United States v. Andreas*, 216 F.3d 645, 680 (7th Cir. 2000) ("The need to negotiate some details of the conspiracy with the cartel members … does not strip a defendant of the organizer role.").

Khan, 522 U.S. 3, 10 (1997). Thus, to succeed on an antitrust claim, a plaintiff must prove that the common scheme designed by the conspirators "constituted an unreasonable restraint of trade either per se or under the rule of reason." *Capital Imaging*, 996 F.2d at 542.

In antitrust cases, "[*p*]*er se* and rule-of-reason analysis are … two methods of determining whether a restraint is 'unreasonable,' *i.e.*, whether its anticompetitive effects outweigh its procompetitive effects." *Atl. Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 342 (1990). Because this balancing typically requires case-by-case analysis, "most antitrust claims are analyzed under [the] 'rule of reason,' according to which the finder of fact must decide whether the questioned practice imposes an unreasonable restraint on competition." *Khan*, 522 U.S. at 10; *see also Gatt Commc'ns, Inc. v. PMC Assocs., L.L.C.*, 711 F.3d 68, 75 n.8 (2d Cir. 2013). However, some restraints "have such predictable and pernicious anticompetitive effect, and such limited potential for procompetitive **[70]** benefit, that they are deemed unlawful *per se*." *Khan*, 522 U.S. at 10. This rule "reflect[s] a longstanding judgment" that case-by-case analysis is unnecessary for certain practices that, "by their nature[,] have a substantial potential" to unreasonably restrain competition. *FTC v. Sup. Ct. Trial Lawyers Ass'n*, 493 U.S. 411, 433 (1990) (internal quotation marks omitted).

Horizontal price-fixing conspiracies traditionally have been, and remain, the "archetypal example" of a *per se* unlawful restraint on trade. *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 647 (1980). By contrast, the Supreme Court in recent years has clarified that vertical restraints—including those that restrict prices—should generally be subject to the rule of reason. *See Leegin*, 551 U.S. at 882 (holding that the rule of reason applies to vertical minimum price-fixing); *Khan*, 522 U.S. at 7 (holding that the rule of reason applies to vertical maximum price-fixing).

In this case, the district court held that the agreement between Apple and the Publisher Defendants was unlawful under the *per se* rule; in the alternative, even assuming that a rule-of-reason analysis was required, the district court concluded that the agreement was still unlawful. *See Apple*, 952 F. Supp. 2d at 694. On appeal, we consider three primary arguments against application of the **[71]** *per se* rule. First, Apple and our dissenting colleague argue that the *per se* rule is inappropriate in this case because Apple's Contracts with the Publisher Defendants were vertical, not horizontal. Even if the challenged agreement here was horizontal, Apple argues next, it promoted "enterprise and productivity." Finally, Apple contends that even if the agreement was horizontal, it was not, in fact, a "price-fixing" conspiracy of the kind that deserves *per se* condemnation. We address, and reject, these arguments in turn. Because the ebook industry, however, is new and at least arguably involves some new ways of doing business, I also consider, writing only for myself, Apple's rule-of-reason argument.

1. Whether the *Per Se* Rule Applies

a. Horizontal Agreement

In light of our conclusion that the district court did not err in determining that Apple organized a price-fixing conspiracy among the Publisher Defendants, Apple and the dissent's initial argument against the *per se* rule—that Apple's conduct must be subject to rule-of-reason analysis because it involved merely multiple independent, vertical agreements with the Publisher Defendants—cannot succeed.

[72] "The true test of legality" under § 1 of the Sherman Act "is whether the *restraint imposed* is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition." *Bd. of Trade of City of Chi. v. United States*, 246 U.S. 231, 238 (1918) (emphasis added). By agreeing to orchestrate a horizontal price-fixing conspiracy, Apple committed itself to "achiev[ing] [that] unlawful objective," *Monsanto*, 465 U.S. at 764 (internal quotation marks omitted): namely, collusion with and among the Publisher Defendants to set ebook prices. This type of agreement, moreover, is a restraint "that would always or almost always tend to restrict competition and decrease output." *Leegin*, 551 U.S. at 886 (internal quotation marks omitted).

The response, raised by Apple and our dissenting colleague, that Apple engaged in "vertical conduct" that is unfit for *per se* condemnation therefore misconstrues the Sherman Act analysis. It is the type of restraint Apple agreed to impose that determines whether the *per se* rule or the rule of reason is appropriate. These rules are means of evaluating "whether [a] *restraint* is unreasonable," not the reasonableness of a particular defendant's role in the scheme. *Atl. Richfield*, 495 U.S. at 342 (emphasis added) (internal quotation marks omitted); *see also Nat'l Collegiate Athletic Ass'n v. Bd. of Regents of the Univ. of Okla.*, **[73]** 468 U.S. 85, 103 (1984) ("Both per se rules and the Rule of Reason are employed to form a judgment about the competitive significance of the restraint." (internal quotation marks omitted)).

Consistent with this principle, the Supreme Court and our Sister Circuits have held all participants in "hub-and-spoke" conspiracies liable when the objective of the conspiracy was a *per se* unreasonable restraint of trade. *See* Richard A. Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. Chi. L. Rev. 6, 22 (1981) ("[C]ases in which dealers or distributors collude … among themselves and bring in the manufacturer to enforce their cartel, … can be dealt with under the conventional rules applicable to horizontal price-fixing conspiracies."). In *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, for example, the Supreme Court considered whether a prominent retailer of electronic appliances could be held liable under § 1 of the Sherman Act for fostering an agreement with and among its distributors to have those companies boycott a competing retailer. 359 U.S. 207 (1959). The Court characterized this arrangement as a "[g]roup boycott[]" supported by a "wide combination consisting of manufacturers, distributors and a retailer." *Id.* at 212-13. It then decided that, if the combination were proved at trial, holding the **[74]** retailer liable would be appropriate because "[g]roup boycotts, or concerted refusals by traders to deal with other traders," are *per se* unreasonable restraints of trade. *Id.* at 212.

The Supreme Court followed a similar approach in *United States v. General Motors Corp.*, 384 U.S. 127 (1966), when it considered whether § 1 prohibited a car manufacturer, General Motors, from coordinating a group of dealerships to prevent other dealers from selling cars at discount prices. The majority called this arrangement a "classic conspiracy in restraint of trade" and refused to entertain General Motors' request to consider the company's reasons for creating the conspiracy. *Id.* at 140. The Court explained that "[t]here can be no doubt that the effect of the combination … here was to restrain trade and commerce within the meaning of the Sherman Act" because "[e]limination, by joint collaborative action, of discounters from access to the market is a per se violation of the Act." *Id.* at 145; *see, e.g.*, *Toys "R" Us*, 221 F.3d at 936; *Denny's Marina, Inc. v. Renfro Prods., Inc.*, 8 F.3d 1217, 1220-21 (7th Cir. 1993); *United States v. MMR Corp. (LA)*, 907 F.2d 489, 498 (5th Cir. 1990); *see also* Albert Foer & Randy Stutz, *Private Enforcement of Antitrust Law in the United States* 29 (2012).

[75] Because the reasonableness of a restraint turns on its anticompetitive effects, and not the identity of each actor who participates in imposing it, Apple and the dissent's observation that the Supreme Court has refused to apply the *per se* rule to certain vertical agreements is inapposite. The rule of reason is unquestionably appropriate to analyze an agreement between a manufacturer and its distributors to, for instance, limit the price at which the distributors sell the manufacturer's goods or the locations at which they sell them. *See Leegin*, 551 U.S. at 881; *Cont'l T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 57 (1977). These vertical restrictions "are widely used in our free market economy," can enhance interbrand competition, and do not inevitably have a "pernicious effect on competition." *Cont'l T.V.*, 433 U.S. at 57-58 (internal quotation marks omitted). But the relevant "agreement in restraint of trade" in this case is not Apple's vertical Contracts with the Publisher Defendants (which might well, if challenged, have to be evaluated under the rule of reason); it is the horizontal agreement that Apple organized among the Publisher Defendants to raise ebook prices. As explained below, horizontal agreements with the purpose and effect of raising prices are *per se* unreasonable because they pose a "threat to the central nervous system of the economy," *United States v. Socony-Vacuum Oil Co.*, 310 U.S. **[76]** 150, 224 n.59 (1940); that threat is just as significant when a vertical market participant organizes the conspiracy. Indeed, as the dissent notes, the Publisher Defendants' coordination to fix prices is uncontested on appeal. *See* Dissenting Op. at 23. The competitive effects of that *same restraint* are no different merely because a different conspirator is the defendant.

Accordingly, when the Supreme Court has applied the rule of reason to vertical agreements, it has explicitly distinguished situations in which a vertical player organizes a horizontal cartel. For instance, in *Business Electronics Corp. v. Sharp Electronics Corp.*, the Court concluded that an agreement "between a manufacturer and a dealer to terminate" another dealer is a "vertical nonprice restraint" that should be evaluated under the rule of reason. 485 U.S. 717, 726 (1988). The Court distinguished *General Motors* and *Klor's* on the grounds that "both cases involved horizontal combinations," *id.* at 734, and noted that "a facially vertical restraint imposed by a manufacturer only because it has been coerced by a 'horizontal carte[l]' … is in reality a horizontal restraint," *id.* at 730 n.4 (alteration in original). More recently, in *NYNEX Corp. v. Discon, Inc.*, the Court ruled that "a buyer's decision to buy from one seller rather than another" is subject to analysis under the rule of reason. 525 U.S. 128, 130 (1998). In **[77]** arriving at this conclusion, the Court took care to distinguish, rather than overturn, *Klor's*, noting that *per se* liability was appropriate for the organizer of the conspiracy in that case because the agreement at issue was not "simply a 'vertical' agreement between supplier and customer, but [also] a 'horizontal' agreement among competitors." *Id.* at 136 (citing *Bus. Elecs. Corp.*, 485 U.S. at 734).

The Court's decision in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, is no different. 551 U.S.

877 (2007). In *Leegin*, a leather manufacturer entered into separate agreements with each of its retailers, which required them to sell its goods at certain prices The plaintiff—a retailer who refused to comply with the requirement—argued that these resale price maintenance agreements constituted *per se* violations of the Sherman Act. The Supreme Court disagreed, concluding that "vertical price restraints are to be judged by the rule of reason." *Id.* at 882. Its analysis was careful to distinguish between vertical restraints and horizontal ones. Vertical price restraints are unfit for the *per se* rule because they can be used to encourage retailers to invest in promoting a product by ensuring that other retailers will not undercut their prices for that good. *See id.* at 890-92. However, vertical price restraints can also be used to organize horizontal cartels [78] to increase prices, which are, "and ought to be, *per se* unlawful." *Id.* at 893. When used for such a purpose, the vertical agreement may be "useful evidence … to prove the existence of a horizontal cartel." *Id.*; *see also* VI Areeda & Hovenkamp, *supra*, ¶ 1402c. The Court made clear that it was addressing only the lawfulness of the manufacturer's vertical agreements and not the plaintiff's claim that the manufacturer also "participated in an unlawful horizontal cartel with competing retailers." *Id.* at 907-08; *see also PSKS, Inc. v. Leegin Creative Leather Prods., Inc.*, 615 F.3d 412 (5th Cir. 2010) (considering plaintiff's "hub-and spoke" theory on remand).

Our dissenting colleague suggests that *Leegin* also "rejected *per se* liability for hub-and-spokes agreements." Dissenting Op. at 18. This position relies on a single sentence from the opinion's analysis of how vertical resale price restraints can harm competition, which states that, if a "vertical agreement setting minimum resale prices is entered upon to facilitate" a horizontal cartel, it "would need to be held unlawful under the rule of reason." *Leegin*, 551 U.S. at 893. If the Supreme Court meant to overturn *General Motors* and *Klor's*—precedents that it has consistently reaffirmed—this cryptic sentence was certainly an odd way to accomplish that result. The Supreme Court "does not normally overturn, or so **[79]** dramatically limit, earlier authority *sub silentio*." *Shalala v. Ill. Council on Long Term Care, Inc.*, 529 U.S. 1, 18 (2000); *see also, e.g.*, *Nestor v. Pratt & Whitney*, 466 F.3d 65, 72 n.8 (2d Cir. 2006) ("It is not within our purview to anticipate whether the Supreme Court may one day overrule its existing precedent." (quoting *United States v. Santiago*, 268 F.3d 151, 155 n.6 (2d Cir. 2001) (internal quotation marks omitted))).

We need not worry about the possibility that *Leegin* covertly changed the law governing hub-and-spoke conspiracies, however, because the passage relied upon by the dissent is entirely consistent with holding the "hub" in such a conspiracy liable for the horizontal agreement that it joins. A horizontal conspiracy can use vertical agreements to facilitate coordination without the other parties to those agreements knowing about, or agreeing to, the horizontal conspiracy's goals. For example, a cartel of manufacturers could ensure compliance with a scheme to fix prices by having every member "require its dealers to adhere to specified resale prices." VIII Areeda & Hovenkamp, *supra*, ¶ 1606b. Because it may be difficult to distinguish such facilitating practices from procompetitive vertical resale price agreements, the quoted passage from *Leegin* notes that those "vertical agreement[s] … would need to be held unlawful under **[80]** the rule of reason." 551 U.S. at 893. But there is no such possibility for confusion in the hub-and-spoke context, where the vertical organizer has not only committed to vertical agreements, but has also agreed to participate in the horizontal conspiracy. In that situation, the court need not consider whether the vertical agreements restrained trade because all participants agreed to the horizontal restraint, which is "and ought to be, *per se* unlawful." *Id.*[20]

In short, the relevant "agreement in restraint of trade" in this case is the price-fixing conspiracy identified by the district court, not Apple's vertical contracts with the Publisher Defendants. How the law might treat Apple's vertical agreements in the absence of a finding that Apple agreed to create the [81] horizontal

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[20] Since *Leegin*, the Sixth Circuit has acknowledged that plaintiffs can "establish[] a *per se* violation [of the Sherman Act] under the hub and spoke theory." *Total Benefits Planning Agency, Inc. v. Anthem Blue Cross & Blue Shield*, 552 F.3d 430, 435 n.3 (6th Cir. 2008). To the extent that the Third Circuit decided otherwise in *Toledo Mack Sales & Serv., Inc. v. Mack Trucks, Inc.*, 530 F.3d 204, 225 (3d Cir. 2008), its more recent opinions cast doubt on that decision. In *In re Insurance Brokerage Antitrust Litigation*, for example, the court noted that "hub-and-spoke conspiracies" have "a long history in antitrust jurisprudence," and cited *Total Benefits* for the position that "[t]he critical issue for establishing a *per se* violation with the hub and spoke system is how the spokes are connected to each other." 618 F.3d 300, 327 (3d Cir. 2010) (internal quotation marks omitted). The court also acknowledged that "[t]he anticompetitive danger inherent" in alleged horizontal collusion "is not necessarily mitigated by the fact that" a broker at a different level of the market structure "managed the details of each bid, nor by the likelihood that the horizontal collusion would not have occurred without the broker's involvement." *Id.* at 338. The panel in *Insurance Brokerage*, however, had no occasion to revisit *Toledo Mack* because the plaintiffs had failed to establish a horizontal agreement—the "rim" in the hub-and-spokes conspiracy. *Id.* at 362.

restraint is irrelevant. Instead, the question is whether the vertical organizer of a horizontal conspiracy designed to raise prices has agreed to a restraint that is any less anticompetitive than its co-conspirators, and can therefore escape *per se* liability. We think not. Even in light of this conclusion, however, we must address two additional arguments that Apple raises against application of the *per se* rule.

b. "Enterprise and Productivity"

Apple seeks refuge from the *per se* rule by invoking a line of cases in which courts have permitted defendants to introduce procompetitive justifications for horizontal price-fixing arrangements that would ordinarily be condemned *per se* if those agreements "when adopted could reasonably have been believed to promote 'enterprise and productivity.'" Apple Br. at 50 (quoting *In re Sulfuric Acid Antitrust Litig.*, 703 F.3d 1004, 1011 (7th Cir. 2012)) (internal quotation mark omitted). The decisions falling in this line are narrow, and they do not support Apple's position. In *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.* ("*BMI*"), the defendants were corporations formed by copyright owners to negotiate "blanket licenses" allowing licensees to perform any of the licensed works for a flat fee. 441 U.S. 1, 4-6 (1979). Although this scheme literally [82] amounted to "price fixing" by the defendants' members, the Court upheld it under the rule of reason because blanket licenses were the only way to eliminate the "prohibitive" cost of each copyright owner's individually negotiating licenses, monitoring licensees' use of their work, and enforcing the licenses' terms. *Id.* at 20-21. In *National Collegiate Athletic Ass'n v. Board of Regents of the University of Oklahoma* ("*NCAA*"), the Court relied on *BMI* in applying the rule of reason to (but ultimately striking down) restrictions placed by the National Collegiate Athletic Association ("NCAA") on the number of football games that its members could agree with television networks to broadcast. 468 U.S. 85, 103 (1984). Many of the NCAA's restrictions on its members were "essential if the product [amateur athletics] is to be available at all," so a "fair evaluation" of the broadcast restrictions' "competitive character require[d] consideration of the NCAA's justifications for the restraints." *Id.* at 101, 103.

The Supreme Court has characterized these decisions as limited to situations where the "restraints on competition are essential if the product is to be available at all." *Am. Needle, Inc. v. Nat'l Football League*, 560 U.S. 183, 203 (2010) (quoting *NCAA*, 468 U.S. at 101) (internal quotation marks omitted). But even if read broadly, these cases, and others in this category, apply the rule of [83] reason only when the restraint at issue was imposed in connection with some kind of potentially efficient joint venture. XI Areeda & Hovenkamp, *supra*, ¶ 1908b; *see, e.g.*, *Sulfuric Acid*, 703 F.3d at 1013 (describing joint venture formed by defendants). Put differently, a participant in a price-fixing agreement may invoke only certain, limited *kinds* of "enterprise and productivity" to receive the rule of reason's advantages. As the Supreme Court has explained—including in *BMI* itself, *see* 441 U.S. at 8 & n.11—the *per se* rule would lose all the benefits of being "*per se*" if conspirators could seek to justify their conduct on the basis of its purported competitive benefits in every case. Here, there was no joint venture or other similar productive relationship between any of the participants in the conspiracy that Apple joined. Apple also does not claim, nor could it, that creating an ebook retail market is possible only if the participating publishers coordinate with one another on price.

c. Price-Fixing Conspiracy

As noted, the Supreme Court has for nearly 100 years held that horizontal collusion to raise prices is the "archetypal example" of a *per se* unlawful restraint of trade. *Catalano*, 446 U.S. at 647. If successful, these conspiracies concentrate the power to set prices among the conspirators, including the "power to control **[84]** the market and to fix arbitrary and unreasonable prices." *United States v. Trenton Potteries Co.*, 273 U.S. 392, 397 (1927). And even if unsuccessful or "not … aimed at complete elimination of price competition," the conspiracies pose a "threat to the central nervous system of the economy" by creating a dangerously attractive opportunity for competitors to enhance their power at the expense of others. *Socony-Vacuum Oil*, 310 U.S. at 224 n.59 (1940). Thus:

> [P]rice-fixing cartels are condemned per se because the conduct is tempting to businessmen but very dangerous to society. The conceivable social benefits are few in principle, small in magnitude, speculative in occurrence, and always premised on the existence of price-fixing power which is likely to be exercised adversely to the public.… And even if power is usually established while any defenses are not, litigation will be complicated, condemnation delayed, would be price-fixers encouraged to hope for escape, and criminal punishment less justified. Deterrence of a generally pernicious practice would be weakened.

Trial Lawyers Ass'n, 493 U.S. at 434 n.16 (quoting 7 Philip Areeda, *Antitrust Law* ¶ 1509, at 412-13 (1986)).

Apple and its amici argue that the horizontal agreement among the publishers was not actually a "price-fixing" conspiracy that deserves *per se* treatment in the first place. But it is well established that *per se* condemnation is not limited to agreements that literally set or restrict prices. Instead, any conspiracy "formed for the purpose and with the effect of raising, depressing, [85] fixing, pegging, or stabilizing the price of a commodity … is illegal per se," and the precise "machinery employed … is immaterial." *Socony-Vacuum Oil*, 310 U.S. at 223; *see also Catalano*, 446 U.S. at 647-48 (collecting cases); XII Areeda & Hovenkamp, *supra*, ¶ 2022a, d. The conspiracy among Apple and the Publisher Defendants comfortably qualifies as a horizontal price-fixing conspiracy.

As we have already explained, the Publisher Defendants' primary objective in expressly colluding to shift the entire ebook industry to an agency model (with Apple's help) was to eliminate Amazon's $9.99 pricing for new releases and bestsellers, which the publishers believed threatened their short-term ability to sell hardcovers at higher prices and the long-term consumer perception of the price of a new book. They had grown accustomed to a business in which they rarely competed with one another on price and could, at least partially, control the price of new releases and bestsellers by releasing hardcover copies before paperbacks. Amazon, and the ebook, upset that model, and reduced prices to consumers by eliminating the need to print, store, and ship physical volumes. Its $9.99 price point for new releases and bestsellers represented a small loss on a small percentage of its sales designed to encourage consumers to adopt the new technology.

[86] Faced 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. Collectively, the Publisher Defendants accounted for 48.8% of ebook sales in 2010. J.A. 1571. Once organized, they had sufficient clout to demand control over pricing, in the form of agency agreements, from Amazon and other ebook distributors. This control over pricing facilitated their ultimate goal of raising ebook prices to the price caps. *See* VIII Areeda & Hovenkamp, *supra*, ¶ 1606b ("Even when specific prices are not agreed upon, an express horizontal agreement that each manufacturer will use resale price maintenance or other distribution restraints should be illegal. Its only business function is to facilitate price coordination among manufacturers."). In other words, the Publisher Defendants took by collusion what they could not win by competition. And Apple used the publishers' frustration with Amazon's $9.99 pricing as a bargaining chip in its negotiations and structured its Contracts to coordinate their push to raise prices throughout the industry. A coordinated effort to raise prices across the relevant market was present in every chapter of this story.

[87] This conspiracy to raise prices also had its intended effect. Immediately after the Publisher Defendants switched Amazon to an agency model, they increased the Kindle prices of 85.7% of their new releases and 96.8% of their *New York Times* bestsellers to within 1% of the Apple price caps. They also increased the prices of their other ebook offerings. Within two weeks of the move to agency, the weighted average price of the Publisher Defendants' ebooks—which accounted for just under half of all ebook sales in 2010—had increased by 18.6%, while the prices for Random House and other publishers remained relatively stable.

This sudden increase in prices reduced ebook sales by the Publisher Defendants and proved to be durable.

One analysis compared two-week periods before and after the Publisher Defendants took control over pricing and found that they sold 12.9% fewer ebooks after the switch. Another expert for Plaintiffs conducted a regression analysis, which showed that, over a six-month period following the switch, the Publisher Defendants sold 14.5% fewer ebooks than they would have had the price increases not occurred. Nonetheless, ebook prices for the Publisher Defendants over those six months, controlling for other factors, remained 16.8% higher than before the switch. And even Apple's expert [88] produced a chart showing that the Publisher Defendants' prices for new releases, bestsellers, and other offerings remained elevated a full two years after they took control over pricing.

Apple points out that, in the two years following the conspiracy, prices across the ebook market as a whole fell slightly and total output increased. However, when the agreement at issue involves price fixing, the Supreme Court has consistently held that courts need not even conduct an extensive analysis of "market power" or a "detailed market analysis" to demonstrate its anticompetitive character. *FTC v. Ind. Fed'n of Dentists*, 476 U.S. 447, 460 (1986); *see also Nat'l Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 692-93 (1978). The district court's assessment of Apple's and the Publisher Defendants' motives, coupled with the unambiguous increase in the prices of their ebooks, was sufficient to confirm that price fixing was the goal, and the result, of the conspiracy. *See Cal. Dental Ass'n v. FTC*, 526 U.S. 756, 779-80 (1999).

Moreover, Apple's evidence regarding long-term growth and prices in the ebook industry is not inconsistent with the conclusion that the price-fixing conspiracy succeeded in actually raising prices. The popularization of ebooks fundamentally altered the publishing industry by eliminating many of the [89] marginal costs associated with selling books. When Apple launched the iBookstore just two years after Amazon introduced the Kindle, the ebook market was *already* experiencing rapid growth and falling prices, and those trends were expected to continue. J.A. 1630, 1647. The district court found that the Publisher Defendants' collective move to retake control of prices—and to eliminate Amazon's $9.99 price point for new releases and *New York Times* bestsellers—tapped the brakes on those trends, causing prices to rise across their offerings and slowing their sales growth relative to other publishers.[21] No court can presume to know the proper price of an ebook, but the long judicial experience applying the Sherman Act has shown that "[a]ny combination which tampers with price structures … would be directly interfering with the free play of market forces." *Socony-Vacuum Oil*, 310 U.S. at 221; *see also Arizona v. Maricopa Cnty. Med. Soc'y*, 457 U.S. 332, 346 (1982). By setting new, durable prices through [90] col-

[21] Significantly, the Publisher Defendants are all major producers of new releases and *New York Times* bestsellers, and they collectively increased prices in those categories. Those prices remained high notwithstanding the influx of new publishers and low-cost ebooks, to the detriment of consumers interested in that segment of the market. *See 42nd Parallel N. v. E St. Denim Co.*, 286 F.3d 401, 405-06 (7th Cir. 2002) ("The key inquiry in a market power analysis is whether the defendant has the ability to raise prices without losing its business." (internal quotation marks omitted)); *K.M.B. Warehouse Distribs., Inc. v. Walker Mfg. Co.*, 61 F.3d 123, 128-29 (2d Cir. 1995); *cf.* U.S. Dep't of Justice & Fed. Trade Comm'n, *Horizontal Merger Guidelines* § 6.1 (2010) (noting that, "[i]n differentiated product industries, some products can be very close substitutes … while other products are more distant substitutes").

lusion rather than competition, Apple and the Publisher Defendants imposed their view of proper pricing, supplanting the market's free play. This evidence, viewed in conjunction with the district court's findings as to and analysis of the conspiracy's history and purpose, is sufficient to support the conclusion that the agreement to raise ebook prices was a *per se* unlawful price-fixing conspiracy.

2. Rule of Reason

As explained above, neither Apple nor the dissent has presented any particularly strong reason to think that the conspiracy we have identified should be spared *per se* condemnation. My concurring colleague would therefore affirm the district court's decision on that basis alone. I, too, believe that *per se* condemnation is appropriate in this case and view Apple's sloganeering references to "innovation" as a distraction from the straightforward nature of the conspiracy proven at trial. Nonetheless, I am mindful of Apple's argument that the nascent ebook industry has some new and unusual features and that the *per se* rule is not fit for "business relationships where the economic impact of certain practices is not immediately obvious." *Leegin*, 551 U.S. at 887 (internal quotation marks omitted); *accord Major League Baseball Props., Inc. v. Salvino, Inc.*, 542 F.3d 290, 316 (2d Cir. 2008) ("*Per se* treatment is not appropriate … where the **[91]** economic and competitive effects of the challenged practice are unclear."); *Sulfuric Acid*, 703 F.3d at 1011 ("It is a bad idea to subject a novel way of doing business … to per se treatment under antitrust law."). I therefore assume, for the sake of argument, that it is appropriate to apply the rule of reason and to analyze the competitive effects of Apple's horizontal agreement with the Publisher Defendants.

Notably, however, the ample evidence here concerning the purpose and effects of Apple's agreement with the Publisher Defendants affects the scope of the rule-of-reason analysis called for in this case. Under a prototypically robust rule-of-reason analysis, the plaintiff must demonstrate an "*actual* adverse effect" on competition in the relevant market before the "burden shifts to the defendants to offer evidence of the procompetitive effects of their agreement." *Geneva Pharms. Tech. Corp. v. Barr Labs. Inc.*, 386 F.3d 485, 506-07 (2d Cir. 2004) (internal quotation marks omitted). The factfinder then weighs the competing evidence "to determine if the effects of the challenged restraint tend to promote or destroy competition." *Id.* at 507. But not every case that requires rule of reason analysis "is a candidate for plenary market examination." *Cal. Dental Ass'n*, 526 U.S. at **[92]** 779. "What is required, rather, is an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint." *Id.* at 781.

To that end, the Supreme Court has applied an abbreviated version of the rule of reason—otherwise known as "quick look" review—to agreements whose anticompetitive effects are easily ascertained. *See id.* at 779. This "quick look" effectively relieves the plaintiff of its burden of providing a robust market analysis, *see id.*, by shifting the inquiry directly to a consideration of the defendant's procompetitive justifications. *See* XI Areeda & Hovenkamp, *supra*, ¶ 1914d ("[W]hen the restraint appears 'on its face' to be one that tends to … increase price," an abbreviated rule-of-reason analysis "operates to shift the burden of proof rather than to cut off the inquiry, as is usually true in a per se case."). Thus, in *NCAA*, the Supreme Court refrained from applying the *per se* rule to the challenged television broadcast restrictions, but it did not require an "elaborate industry analysis … to demonstrate [their] anticompetitive character." 468 U.S. at 109 (internal quotation marks omitted). And in *Indiana Federation of Dentists*, the Court did not apply the *per se* rule to a group boycott when, in the relevant market, the economic impact was "not immediately obvious," but it nonetheless dispensed with a full analysis of the agreement's **[93]** anticompetitive character. 476 U.S. at 459; *see also Major League Baseball*, 542 F.3d at 317; *United States v. Brown Univ.*, 5 F.3d 658, 669 (3d Cir. 1993).

Here, the same evidence supporting our determination that *per se* condemnation is the correct way to dispose of this appeal also supports at most a "quick look" inquiry under the rule of reason. Contrary to the dissent's suggestion, this approach does not somehow "taint" the rule-of-reason analysis. The dissent concedes that the conscious object of Apple's signing its Contracts with the Publisher Defendants was to organize a horizontal conspiracy among them to raise consumer-facing ebook prices. *See* Dissenting Op. at 26 (noting that "price increases" were "the expected result" of the defendants' agreement). It is unsurprising in these circumstances that we are easily able to discern the anticompetitive effects of that horizontal conspiracy. A quick-look approach operates only to shift the rule-of-reason analysis directly to Apple's procompetitive justifications for organizing the conspiracy; I do not give those defenses any shorter shrift than I otherwise would under a more robust analysis. My rejection of Apple's defenses thus has nothing to do with my application of the quick-look approach and everything to do with how unpersuasive those defenses are.

[94]

a. Market Entry

Apple's initial argument that its agreement with the Publisher Defendants was procompetitive (an argument presented principally in an amicus brief adopted wholeheartedly by the dissent) is that by eliminating Amazon's $9.99 price point, the agreement enabled Apple and other ebook retailers to enter the market and challenge Amazon's dominance. But this defense—that higher prices enable more competitors to enter a market—is no justification for a horizontal price-fixing conspiracy. As the Supreme Court has cogently explained:

> [I]n any case in which competitors are able to increase the price level or to curtail production by agreement, it could be argued that the agreement has the effect of making the market more attractive to potential new entrants. If that potential justifies horizontal agreements among competitors imposing one kind of voluntary restraint or another on their competitive freedom, it would seem to follow that the more successful an agreement is in raising the price level, the safer it is from antitrust attack. Nothing could be more inconsistent with our cases.

Catalano, 446 U.S. at 649.

Nor does this argument become stronger when it is asserted, as here, that a horizontal cartel at one level of the market promoted market entry at another, enhancing competition. My dissenting colleague's view that "deconcentrating," **[95]** Dissenting Op. at 27, Amazon's share of retail ebook sales justifies *concentrating* power over pricing in the hands of the Publisher Defendants reflects a basic misunderstanding of the nature of the competition that antitrust law protects. New entrants to a market are desirable to the extent that consumers would choose to buy their products at the price offered. When a market is concentrated and an incumbent firm is charging supracompetitive prices, a new entrant can benefit consumers by undercutting the incumbent's prices, thus offering better value for the same goods. Dominant firms who want to deter competition—so that they can keep charging supracompetitive prices—may erect barriers to entry to keep these new competitors out, and the dissent is quite right that these barriers are generally undesirable.

Market dominance may, however, arise "as a consequence of a superior product, business acumen, or historic accident," and is "not only not unlawful; it is an important element of the free market system." *Trinko*, 540 U.S. at 407 (internal quotation marks omitted). The ability to provide goods at particularly low prices is one way that a firm can gain such an edge in the marketplace. Competitors are, of course, entitled to challenge dominant firms by offering, among other things, superior products and lower prices. But success is not **[96]** guaranteed. A dominant firm charging low prices may have proven itself more efficient than its competitors, such that a potential new entrant's inability to earn a profit would result not from any artificial "barriers to entry," but rather from the fact that, in light of the value proposition offered by the dominant firm, consumers would not choose to buy the new entrant's products at the price it is willing and able to offer. *See* Einer Elhauge, *United States Antitrust Law and Economics* 2 (2d ed. 2011) ("If a firm makes a better mousetrap, and the world beats a path to its door, it may drive out all rivals and establish a monopoly; but that is a good result, not a bad one.").

From this perspective, the dissent's contention that Apple could not have entered the ebook retail market without the price-fixing conspiracy, because it could not have profited either by charging more than Amazon or by following Amazon's pricing, is a complete non sequitur. The posited dilemma is the whole point of competition: if Apple could not turn a profit by selling new releases and bestsellers at $9.99, or if it could not make the iBookstore and iPad so attractive that consumers would pay *more* than $9.99 to buy and read those ebooks on its platform, then there was no place for its platform in the ebook retail market. Neither the district court nor Plaintiffs had an obligation to identify a "viable **[97]** alternative" for Apple's profitable entry because Apple had no entitlement to enter the market on its preferred terms. Dissenting Op. at 35.

Although low prices that deter new entry may simply reflect the dominant firm's efficiency, it is true that below-cost pricing can, under certain circumstances, be anticompetitive. The dissent suggests that Amazon's pricing gave it an unfair advantage, so that even if Apple had priced ebooks at an efficient level (whatever that might have been), it still would not have been able to enter the market on a profitable basis. But Amazon was taking a risk by engaging in loss-leader pricing, losing money on some sales in order to encourage readers to adopt the Kindle. "That below-cost pricing may impose painful losses on its target is of no moment to the antitrust laws if competition is not injured: It is axiomatic that the antitrust laws were passed for 'the protection of *competition*, not *competitors*.'" *Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 224 (1993) (quoting *Brown Shoe Co. v. United*

States, 370 U.S. 294, 320 (1962)). Because lower prices improve consumer welfare (all else being equal), below-cost pricing is unlawfully anticompetitive only if there is a "dangerous probability" that the firm engaging in it will later recoup its losses by raising prices to monopoly levels after driving its rivals out of the market. *Id.* If **[98]** Apple and the Publisher Defendants thought that Amazon's conduct was truly anticompetitive under this standard, they could have sued under § 2 of the Sherman Act. (Whether DOJ would have pursued its own enforcement action is of unclear relevance given the availability of a private remedy.) Failing that, Amazon's pricing was part of the competitive landscape that competing ebook retailers had to accept.[22]

Instead, the dissent invites conduct that is strictly prohibited by the Sherman Act—horizontal collusion to fix prices—to cure a perceived abuse of market power. Whatever its merit in the abstract, that preference for collusion over dominance is wholly foreign to antitrust law. *See Trinko*, 540 U.S. at 408 (referring to collusion as the "supreme evil of antitrust"). Because of the long-term threat to competition, the Sherman Act does not authorize horizontal price conspiracies as a form of marketplace vigilantism to eliminate perceived "ruinous competition" or other "competitive evils." *Maricopa Cnty. Med. Soc'y*, 457 U.S. at 346 (quoting *Socony-Vacuum Oil*, 310 U.S. at 221). Indeed, the attempt to justify a conspiracy to raise prices "on the basis of the potential threat that **[99]** competition poses … is noth-

[22] While the dissent accuses us of supposing that "competition should be genteel, lawyer-designed, and fair under sporting rules," Dissenting Op. at 5, it is the dissent's position that would have ebook consumers subsidize Apple's entry into the market by paying more for ebooks so that Apple would not have to compete on price.

ing less than a frontal assault on the basic policy of the Sherman Act." *Nat'l Soc'y of Prof'l Eng'rs*, 435 U.S. at 695. And it is particularly ironic that the "terms" that Apple was able to insist upon by organizing a cartel of Publisher Defendants to move against Amazon—namely, the elimination of retail price competition—accomplished the precise opposite of what new entrants to concentrated markets are ordinarily supposed to provide. In short, Apple and the dissent err first in equating a symptom (a single-retailer market) with a disease (a lack of competition), and then err again by prescribing the disease itself as the cure.

The dissent's "frontal assault" on competition law is not only wrong as a legal matter for all the reasons just given; it is also, despite its professed fidelity to the district court's view of the facts, premised on various mischaracterizations of the record. Put simply, it is far from clear that either Apple itself or other ebook retailers could not have entered the ebook retail market without Apple's efforts with the Publisher Defendants to eliminate price competition. As the district court noted, "[Apple] did not attempt to argue or show at trial that the price of admission to new markets must be or is participation in illegal price fixing schemes" and did not "suggest[] that the only way it could have entered **[100]** the e-book market was to agree with the Publisher Defendants to raise e-book prices." *Apple*, 952 F. Supp. 2d at 708.

The district court's statement that Apple feared "losing money if it tried or was forced to match Amazon's pricing," *Id.* at 658—the peg on which the dissent largely hangs its argument—is hardly a conclusive finding that Apple would have lost money had it entered a market that featured retail price competition. Barnes & Noble, for its part, had chosen to enter and stay in the market in the face of Amazon's pricing. Google, too, had plans to enter the ebook market before Apple launched the iBookstore. Moreover, the district court never found that Apple could not have entered the market on a wholesale model while charging *more* than Amazon for new releases and bestsellers. To fill this hole in its theory, the dissent suggests that Apple would have "impair[ed] its brand" by charging more than Amazon. Dissenting Op. at 34 (internal quotation marks omitted). But putting aside the fact that Apple's perception of its brand value is irrelevant—does the dissent really think 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?—the district court actually found that Apple believed it would have been "unrealistic[]" to **[101]** charge more than its *price caps* after switching to an agency model, *Apple*, 952 F. Supp. 2d at 692, a finding that says nothing about what Apple would have been willing to charge under a wholesale model.

The record makes clear the flaws in the dissent's argument. When Cue was still contemplating a wholesale model, his objective was not for Apple's pricing to match Amazon's precisely, but rather for that pricing to be "generally competitive." J.A. 1758. And had Apple opted to compete on both price and platform but concluded that it could not match Amazon's $9.99 pricing, some consumers might well have paid somewhat more to read new releases and bestsellers on the iPad, a revolutionary ereader boasting many more features than the Kindle.[23] The iPad was coming to market with or

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[23] A prediction that consumers would have paid more to read ebooks on the iPad than on the Kindle because of the iPad's im-

without a price-fixing **[102]** conspiracy, and some iPad owners who wanted to read ebooks surely would not have wanted to buy a separate Kindle solely to benefit from Amazon's $9.99 pricing for new releases and best-sellers. (Whether Apple would have viewed its profits under that scenario as large enough to justify entry is not an antitrust concern.)

In actuality, the district court's fact-finding illustrates that Apple organized the Publisher Defendants' price-fixing conspiracy not because it was a necessary precondition to market entry, but because it was a convenient bargaining chip. Apple was operating under a looming deadline and recognized that, by aligning its interests with those of the Publisher Defendants and offering them a way to raise prices across the ebook market, it could gain quick entry into the market on extremely favorable terms, including the elimination of

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proved reading experience or other attractive features does not somehow suggest that ebooks are "Veblen goods [or] Giffen goods." Dissenting Op. at 33 n.7. The dissent also suggests that Apple could not have depended on the iPad's hardware advantages as part of a strategy to charge more than Amazon because antitrust law would have required it to open up the iPad to a Kindle app. *Id.* at 34. But for a unilateral refusal to deal to be unlawful, the defendant must have monopoly power, which Apple plainly did not. *See, e.g.*, *United States v. Microsoft Corp.*, 253 F.3d 34, 51 (D.C. Cir. 2001) (en banc) ("While merely possessing monopoly power is not itself an antitrust violation, it is a necessary element of a monopolization charge." (citation omitted)); Elhauge, *supra*, at 268 ("A firm that lacks dominant market power … can unilaterally choose with whom they deal without fear of antitrust liability."); *see also Trinko*, 540 U.S. at 408 ("Under certain circumstances, a refusal to cooperate with rivals can constitute anticompetitive conduct and violate § 2. We have been very cautious in recognizing such exceptions, because of the uncertain virtue of forced sharing and the difficulty of identifying and remedying anticompetitive conduct by a single firm.").

retail price competition from Amazon. But the offer to orchestrate a horizontal conspiracy to raise prices is not a legitimate way to sweeten a deal.

The facts also do not support the conclusion that Amazon's market position would have discouraged other ebook retailers from entering the market absent the price-fixing conspiracy orchestrated by Apple. Amazon popularized **[103]** ebooks with the launch of the Kindle in late 2007, and enjoyed a strong market position because of its innovation. *Cf. Trinko*, 540 U.S. at 407 (noting that the opportunity to gain market power "induces risk taking that produces innovation and economic growth"). Barnes & Noble was Amazon's first major competitor, and when it entered the market—on a wholesale model—with the introduction of the Nook in 2009, it began to erode Amazon's market share. The iPad itself also promised to introduce more competition with or without Apple's iBookstore by providing a platform for companies to build ebook marketplaces without investing in tablet development. These new entrants gave publishers more leverage to negotiate for alternative sales models or different pricing. Indeed, publishers were already in separate discussions about an agency model with Barnes & Noble before Apple offered a way to swap the rigors of competition for the comfort of collusion.

To summarize, the district court made no finding that a horizontal conspiracy to eliminate price competition in the ebook retail market was necessary to bring more retailers into the market to challenge Amazon, nor does the record evidence support this conclusion. More importantly, even if there *were* such evidence, the fact that a competitor's entry into the market is **[104]** contingent on a horizontal conspiracy to raise prices only means (absent monopolistic conduct by the market's dominant firm, which cannot lawfully be challenged by collusion) that the competitor is inefficient, *i.e.*, that its entry will not enhance consumer welfare. For these reasons, I would reject the argument that Apple's entry into the market represented an important procompetitive benefit of the horizontal price-fixing conspiracy it orchestrated.

b. Other Justifications

Apart from its and other retailers' entry into the market, Apple points to other purported procompetitive benefits of its agreement with the Publisher Defendants, namely, eventual price decreases in the ebook industry and the various technological innovations embedded in the iPad. The district court correctly concluded that Apple failed to establish a connection between these benefits and the conspiracy among Apple and the Publisher Defendants. *Apple*, 952 F. Supp. 2d at 694; *see NCAA*, 468 U.S. at 113-15 (concluding that the need to coordinate to produce intercollegiate athletics was not related to coordination on television rights); XI Areeda & Hovenkamp, *supra*, ¶ 1908b.

While it may be true that ebook prices eventually declined industry-wide, new publishers were adopting the digital format and prices were falling even **[105]** before Apple's entry into the market. Apple did not introduce any admissible evidence linking the continued influx of new titles into the ebook market to its agreement with the Publisher Defendants.[24] Nor did it

[24] Apple sought to introduce expert testimony from Dr. Michelle Burtis, which it believed would link continued long-term growth and price changes to its launch of the iBookstore. However, the district court excluded this testimony on the grounds that Dr. Burtis "did not offer any scientifically sound analysis of the cause for this purported price decline or seek to control for the

provide an explanation for how this price-fixing agreement altered the business and pricing decisions of other publishers in a procompetitive direction. The district court's refusal to give Apple credit for these trends was therefore proper.

The technological innovations embedded in the iPad are similarly unrelated to Apple's agreement with the Publisher Defendants. The iPad's backlit touchscreen, audio and video capabilities, and ability to offer consumers a number of services on a single device revolutionized tablet computing. But, as **[106]** Apple's witnesses testified, the company had every intention of bringing the iPad to market with or without the iBookstore. Moreover, Apple was not the only entity that could use the iPad's new features to enhance the ebook experience—other retailers, or the publishers themselves, could have designed and launched ebook applications on the platform. The district court was correct not to score these hardware innovations as pro-

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factors that may have led to it." *Apple*, 952 F. Supp. 2d at 694 n.61. This was no abuse of discretion. *See Zerega Ave. Realty*, 571 F.3d at 212-13. "[T]he proponent of expert testimony has the burden of establishing by a preponderance of the evidence" that the expert's opinion is based on sufficient facts, is the product of reliable principles and methods, and applies those principles and methods reliably to the facts at hand. *United States v. Williams*, 506 F.3d 151, 160 (2d Cir. 2007); *see* Fed. R. Evid. 702. Dr. Burtis merely compared the average ebook prices from the two years before Apple's entry into the market with the average prices two years after. She did not account for the rapid growth and change in that industry or explain the process she used to determine whether Apple's agency agreements were responsible for lower prices. *See Gen. Elec. Co. v. Joiner*, 522 U.S. 136, 146 (1997); *United States v. Dukagjini*, 326 F.3d 45, 54 (2d Cir. 2003). The district court therefore acted well within its discretion in excluding Dr. Burtis's testimony.

competitive benefits of the agreement between Apple and the Publisher Defendants to raise prices.

Accordingly, I agree with the district court's decision that, under the rule of reason, the horizontal agreement to raise consumer-facing ebook prices that Apple orchestrated unreasonably restrained trade. But given the clear applicability of the *per se* rule in this context, the analysis here is largely offered in response to the dissent. I also confidently join with my concurring colleague in affirming the district court's conclusion that Apple committed a *per se* violation of § 1 of the Sherman Act.

III. The Injunctive Order

Next, Apple and two of the Publisher Defendants—Macmillan and Simon & Schuster—challenge specific portions of the district court's September 5, 2013 injunctive order. In particular, Macmillan and Simon & Schuster ask us to vacate **[107]** the provision which prohibits Apple, for a period of time, from entering agreements with the Publisher Defendants that restrict its ability to set ebook prices. S.P.A. 205. Apple separately seeks vacatur of a provision requiring it to apply the same terms and conditions to ebook applications in its App Store as it does to other applications, and of the district court's decision to appoint a compliance monitor. We address each of the parties' arguments in turn.

A. Macmillan and Simon & Schuster

In the September 5, 2013 injunctive order, the district court mandated that "Apple shall not enter into or maintain any agreement with a Publisher Defendant that restricts, limits, or impedes Apple's ability to set, alter, or reduce the Retail Price of any E-book or to offer price discounts or any other form of promotions.

S.P.A. 205. This prohibition began upon entry of the order and expires at different times for each of the Publisher Defendants. The earliest expiration date lifts the ban for agreements between Apple and Hachette beginning 24 months after entry of the injunctive order. Expiration dates for agreements with each of the other Publisher Defendants are then set in six-month intervals, with Simon & Schuster's ban expiring 36 months after entry of the final judgment and Macmillan's ban ending after 48 months.

[108] Macmillan and Simon & Schuster seek vacatur of this prohibition. Both publishers are subject to separate consent decrees, which prohibit them from signing agreements with *any* ebook retailers which restrict the retailer's ability to "set, alter, or reduce" ebook prices, "or to offer price discounts." J.A. 1126; J.A. 1148. The prohibition lasts two years for Simon & Schuster and 23 months for Macmillan. According to both Publisher Defendants, the district court's injunctive order against Apple, in light of these consent decrees, is unlawful for two reasons. First, they contend that the injunctive order impermissibly *modifies* their consent decrees by extending the time during which they cannot negotiate to restrict the price at which Apple sells ebooks.[25] Second, they argue that DOJ should have been judicially estopped from seeking a prohibition on agreements limiting Apple's discounting authority that lasts longer than two years because, in the filings in support of the consent decrees, it argued that two years was a sufficient amount of time to restore

[25] Macmillan also contends that the injunctive order broadens the restrictions imposed by its consent decree because the decree allows the company to set certain limits on price discounts, which it can no longer set for ebooks sold by Apple.

competition in the ebook market. Neither objection is persuasive.

[109] We begin with the argument that the injunctive order impermissibly amended the Publisher Defendants' consent decrees. Federal Rule of Civil Procedure 60(b) establishes the grounds for seeking "relief from a final judgment, order, or proceeding," Fed. R. Civ. P. 60(b), including modifications of consent decrees. *Rufo v. Inmates of Suffolk Cnty. Jail*, 502 U.S. 367, 378-79 (1992); *United States v. Eastman Kodak Co.*, 63 F.3d 95, 101 (2d Cir. 1995). The rule adopts a flexible approach, enumerating specific reasons for modification while also allowing alterations for "any other reason that justifies relief." Fed. R. Civ. P. 60(b). "[A] party seeking an alteration" under this catch-all provision bears the "burden of establishing that a significant change in circumstances warrants the modification." *United States v. Sec'y of Hous. & Urban Dev.*, 239 F.3d 211, 217 (2d Cir. 2001).

The Publisher Defendants' argument rests on the premise that the district court's injunctive order modified their consent decrees and therefore should have complied with Rule 60(b)'s requirements. The premise is incorrect. Macmillan's and Simon & Schuster's consent decrees prohibit them from restricting any retailer's authority to set prices. The injunctive order does not alter the terms of those decrees. Instead, it provides relief against a *different* party **[110]** by limiting Apple's authority to negotiate away its ability to set prices in agreements with any of the Publisher Defendants. The fact that the order also has the effect of preventing the Publisher Defendants from restricting Apple's pricing authority does not render it "[r]elief from a final judgment, order, or proceeding" requiring a motion under Rule 60(b). Fed. R. Civ. P. 60(b). A consent decree is "enforced as [an] order[]," but "construed largely as [a] contract[]." *SEC v. Citigroup Global Mkts., Inc.*, 752 F.3d 285, 297 (2d Cir. 2014) (internal quotation marks omitted). Its scope must be discerned within its "four corners, and not by reference to what might satisfy the purposes of one of the parties to it." *United States v. Armour & Co.*, 402 U.S. 673, 682 (1971); *see also Perez v. Danbury Hosp.*, 347 F.3d 419, 424 (2d Cir. 2003). An injunctive order against an entity that is not party to the consent decree and neither changes the terms of nor interprets the decree does not modify the contract and therefore does not require a Rule 60(b) motion. Indeed, as a practical matter, injunctions often alter the options available to other parties. Rule 60(b) does not hold district courts issuing injunctions to a higher standard simply because the injunction may affect rights addressed in a different party's consent decree.

[111] Macmillan and Simon & Schuster's judicial estoppel argument fares no better. Judicial estoppel is "invoked by a court at its discretion," and is designed to "protect the integrity of the judicial process by prohibiting parties from deliberately changing positions according to the exigencies of the moment." *New Hampshire v. Maine*, 532 U.S. 742, 749-50 (2001) (citation omitted) (internal quotation marks omitted). While the propriety of applying estoppel depends heavily on the "specific factual context[]" before the court, we typically consider whether the party's argument is "clearly inconsistent with its earlier position," whether the party "succeeded in persuading a court to accept" that earlier position, and whether the "party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped." *Id.* at 750-51 (internal quotation marks omitted); *see also Adelphia Recovery Trust v. Goldman, Sachs & Co.*, 748 F.3d 110, 116 (2d Cir. 2014). "[R]elief is granted only when the … impact on judicial integrity is certain." *Republic of Ecuador v. Chevron Corp.*, 638 F.3d 384, 397 (2d Cir. 2011) (internal quotation marks omitted).

We conclude that DOJ's arguments in support of the injunctive order were neither so clearly inconsistent with its earlier arguments nor so unfairly **[112]** detrimental to the Publisher Defendants as to warrant judicial estoppel. In support of the consent decrees, the Justice Department argued that a two-year ban on restricting retailers' abilities to set prices was sufficient to "allow movement in the marketplace away from collusive conditions." J.A. 1055. It then pushed for a longer, five-year restriction on agreements specifically with Apple. While facially inconsistent, we have emphasized the need to "carefully consider the contexts in which apparently contradictory statements are made to determine if there is, in fact, direct and irreconcilable contradiction." *Rodal v. Anesthesia Grp. of Onondaga, P.C.*, 369 F.3d 113, 119 (2d Cir. 2004). And here, context is particularly important. The consent decrees ban certain agreements between the Publisher Defendants and *any* retailers. The injunctive order, on the other hand, pertained only to the Publisher Defendants' agreements with Apple. Given the extensive factfinding at trial about the relationship that Apple developed with the Publisher Defendants and its willingness to coordinate their conspiracy, DOJ had a basis for distinguishing the length of the restrictions in the consent decrees from those in the injunctive order. This was not a case of a party reversing courses, to the detriment of the legal system, "simply because his interests have changed." *New Hampshire*, 532 U.S. at 749.

[113] Furthermore, the district court did not approve the Justice Department's request for a five-year ban on all discounting restrictions between Apple and the Publisher Defendants. Instead, the injunctive order adopts an interval-based system, which prevents Apple from agreeing to limit its pricing authority for between 24 and 48 months depending on the Publisher Defendant. The district court imposed this interval system so "there would be no point in time when Apple would be renegotiating with all of the publisher defendants at once[, and] no one point in time when [a] publisher defendant[] could be assured that it was taking the same bargaining position as its peers vis-à-vis Apple." J.A. 2376. This independent rationale for the injunctive order ensures that DOJ's argument did not produce "inconsistent results" or compromise the integrity of the judicial process. *Simon v. Safelite Glass Corp.*, 128 F.3d 68, 72 (2d Cir. 1997).

[114]

B. Apple

Apple, like Macmillan and Simon & Schuster, objects to the portion of the injunctive order preventing it from agreeing to limit its pricing authority. In addition, the company asks us to vacate another provision, which requires it to "apply the same terms and conditions to the sale or distribution of an E-book App through Apple's App Store as [it] applies to all other apps sold or distributed through [the] App Store." S.P.A. 207. Apple contends that neither provision is necessary to protect the public.[26] We disagree.

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[26] Apple also argues that the district court's decision to appoint a monitor to supervise the company's compliance with the injunction went beyond its powers under the Sherman Act and

[115] "A Government plaintiff, unlike a private plaintiff, must seek to obtain relief necessary to protect the public from *further* anticompetitive conduct and to

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violated both Federal Rule of Civil Procedure 53 and separation of-powers principles. Apple devoted only two conclusory sentences to these three separate facial challenges to the district court's authority. We therefore deem the arguments forfeited and do not consider them. *Frank v. United States*, 78 F.3d 815, 833 (2d Cir. 1996) ("Issues not sufficiently argued are in general deemed waived and will not be considered on appeal."), *vacated on other grounds*, 521 U.S. 1114 (1997); *Zhang v. Gonzales*, 426 F.3d 540, 545 n.7 (2d Cir. 2005). We also note that, following Rule 53's amendment in 2003, the Advisory Committee stated that "[r]eliance on a master" appointed under that Rule "is appropriate when a complex decree requires complex policing, particularly when a party has proved resistant or intransigent," and that both the Supreme Court and this Court have approved such appointments. Fed. R. Civ. P. 53 advisory committee's note (2003 Amendments) (citing *Local 38 of the Sheet Metal Workers' Int'l Ass'n v. E.E.O.C.*, 478 U.S. 421, 481-82 (1986)); *see also Republic of the Philippines v. N.Y. Land Co.*, 852 F.2d 33, 36-37 (2d Cir. 1988) (collecting cases). In light of this background, it would be inappropriate to excuse Apple's failure to argue and for this panel to entertain its facial challenges to the district court's authority on the scant briefing before us.

Judge Jacobs, who sat on a separate panel of this Court that considered an as-applied challenge to the monitor's conduct, contends that "the injunction warps the role of a neutral, court-appointed referee into that of an adversary party." Dissenting Op. at 36. Whatever the merits of this argument, it is not properly before us on this appeal. Here, Apple has asserted only (and without argumentation of any sort) that appointing a monitor, *in general*, violates the Sherman Act, Rule 53, and separation-of-powers principles. The dissent's position eschews that broad facial challenge and instead focuses on the conduct of the monitor in this *particular* case, drawing entirely on a record not before this panel, but presented to a *separate* panel in another appeal. *See United States v. Apple Inc.*, 2015 WL 3405534 (2d Cir. 2015). We do not believe it is proper to resolve this appeal with reference to arguments that Apple has failed to make.

redress anticompetitive harm." *F. Hoffmann-La Roche Ltd. v. Empagran S.A.*, 542 U.S. 155, 170 (2004) (emphasis added). Thus, "[w]hen the purpose to restrain trade appears from a clear violation of law, it is not necessary that all untraveled roads to that end be left open and that only the worn one be closed." *Int'l Salt Co. v. United States*, 332 U.S. 392, 400 (1947), *abrogated on other grounds by Ill. Tool Works Inc. v. Independent Ink, Inc.*, 547 U.S. 28 (2006). The district court has "large discretion to model [its] judgments to fit the exigencies of the particular case," *id.*, and "all doubts" about the remedy are to be "resolved in [the Government's] favor," *United States v. E.I. du Pont de Nemours & Co.*, 366 U.S. 316, 334 (1961).

The district court was well within its discretion to restrict Apple's ability to give up its pricing authority and to require that Apple treat ebook applications the same way that it treats other applications. Apple relinquished its authority to **[116]** set prices as part of its conspiracy with the Publisher Defendants. By delaying Apple's ability to renegotiate similar restrictions and arranging for the restrictions to expire at different times for each Publisher Defendant, the injunctive order ensured that Apple and the Publisher Defendants would not be able to use that same strategy as part of a new conspiracy. The provision requiring ebook applications in the App Store to receive the same terms and conditions as other applications furthers that goal. The district court expressed concern that Apple and the Publisher Defendants may use ebook applications to circumvent the injunction's rules about Apple's pricing authority, or that Apple may impose restrictions on ebook applications to punish publishers who refused to act in concert with their competitors. For instance, the court found evidence that Random House eventually joined the iBookstore on Apple's desired terms in part because Apple prevented the company from launching an ebook application in the App Store. The district court was therefore correct to decide that these provisions of the injunctive order were "necessary to protect the public from further anticompetitive conduct." *F. Hoffmann-La Roche*, 542 U.S. at 170.

[117]

CONCLUSION

We have considered the appellants' remaining arguments and find them to be without merit. Because we conclude that Apple violated § 1 of the Sherman Act by orchestrating a horizontal conspiracy among the Publisher Defendants to raise ebook prices, and that the injunctive relief ordered by the district court is appropriately designed to guard against future anticompetitive conduct, the judgment of the district court is **AFFIRMED**.

[1] Lohier, *Circuit Judge*, concurring in part and concurring in the judgment:

I join in the majority opinion except for part II.B.2 relating to the application of the rule of reason. In my view, Apple's appeal rises or falls based on the application of the per se rule. That rule clearly applies to the central agreement in this case (and the only agreement alleged to be unlawful): the publishers' horizontal agreement to fix ebook prices. *Cf. Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 893 (2007) (vertical agreements "may … be useful evidence for a plaintiff attempting to prove the existence of a horizontal cartel"). I would affirm on that basis alone.

That said, I recognize that the publisher defendants, who used Apple both as powerful leverage against Amazon and to keep each other in collusive check, may appear to be more culpable than Apple. And there is also some surface appeal to Apple's argument that the ebook market, in light of Amazon's virtually uncontested dominance, needed more competition. But more corporate bullying is not an appropriate antidote to corporate bullying. It cannot have been lawful for Apple to respond to a competitor's dominant market power by helping rival corporations (the publishers) fix prices, as the District Court found happened here. However sympathetic Apple's plight and the publishers' predicament may [2] have been, I am persuaded that permitting "marketplace vigilantism," Majority Op. at 9, would do far more harm to competition than good, would be disastrous as a policy matter, and is in any event not sanctioned by the Sherman Act.

[1] DENNIS JACOBS, *Circuit Judge*, dissenting:

I respectfully dissent.

This appeal is taken by Apple Inc. from a judgment in the United States District Court for the Southern District of New York (Cote, *J.*), awarding an antitrust injunction in favor of the United States, 31 states, the District of Columbia, and the Commonwealth of Puerto Rico. The plaintiffs' claims are premised on Apple's conduct as a prospective retailer of e-books. I vote to reverse.

* * *

I have no quarrel with the district court's conscientious findings of fact; I affirmatively rely on them, and cite them throughout. The 156 pages of findings track communications and interactions that happened over the 48-day course of events, detail by detail. *See United States v. Apple Inc.*, 952 F. Supp. 2d 638, 655-81 (S.D.N.Y. 2013) ("*Apple I*"). All that is needed to decide the case, however, are the schematic facts that show the architecture of the horizontal and vertical arrangements and the dynamics of the competitive forces. They are set out in a [2] nutshell in the following paragraphs, and at somewhat greater length in the Background section of this opinion.

As Apple was preparing the launch of its first iPad tablet in 2009, the company recognized that the device could support e-books, and gave consideration to including an e-book retail platform. However, Amazon had preceded Apple in the market, had established a 90 percent ascendency in sales of e-books, and was effectively excluding new entrants by offering bestsellers at a price ($9.99) that for many books was below the prices Amazon was paying publishers.

Although Apple was positioned to enter the retail market, it was unwilling to do so on terms that would incur a loss on e-book sales (as would happen if it met Amazon's below-cost price), or that would impair its brand and likely fail (as would happen if it charged more than Amazon). So, as a condition to its entry as a competing buyer for the publishers' wares, Apple insisted that the publishers agree to a distribution model that would lower that barrier to retail entry.

The new distribution model was implemented by several terms in Apple's contracts with publishers: agency pricing, tiered price caps, and a most-favored nation clause. It is conceded that none of those terms is, standing alone, illegal. [3] Apple also encouraged publishers to implement agency pricing in their contracts with other retailers. Although publishers were unhappy about Amazon's below cost price for e-books (which eroded the publishers' hardcover sales) no one publisher alone could counter Amazon. In short order, five of the country's six largest publishers agreed to Apple's terms and jointly pressured Amazon to adopt agency pricing. The publishers thereby prevailed in what the district court found to be a horizontal price-fixing conspiracy. The barrier to entry thus removed, Apple entered the retail market as a formidable competitor. In the deconcentrated market, Amazon's 90 percent market share is now 60 percent.

(I acknowledge that, in adducing facts found by the district court, this opinion unavoidably casts imputations on Amazon. Fairness requires acknowledgment that Amazon has not appeared in this litigation and has not had a full opportunity to dispute the district court's findings or characterizations. Moreover, the fact of Amazon's monopoly alone would not support an inference that Amazon's behavior was in any way unlawful.)

The Department of Justice, 31 states, the District of Columbia, and the Commonwealth of Puerto Rico sued Apple and the five publishers for conspiracy in unreasonable restraint of trade, in violation of § 1 of the Sherman Antitrust **[4]** Act, 15 U.S.C. § 1. The publishers settled, and Apple proceeded to a bench trial. The district court ruled that Apple's conduct as a vertical enabler of the publishers' horizontal price conspiracy constituted a violation *per se* of § 1, and that (in any event) Apple's conduct would also violate § 1 under the rule of reason. On this appeal, a majority affirms only on the ground of liability *per se*. *See* Op. of Judge Lohier, *ante*, at 1. Since I would reverse, I consider as well the rule of reason. Judge Livingston's opinion argues (for herself alone) that the judgment could be affirmed on that alternative ground.

The district court committed three decisive errors:

- The district court ruled (and the majority affirms) that a vertical enabler of a horizontal price-fixing conspiracy is in *per se* violation of the antitrust laws. However, the Supreme Court teaches that a vertical agreement designed to facilitate a horizontal cartel "would need to be held unlawful *under the rule of reason*." *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 893 (2007) (emphasis added). **(POINT I)**

- The district court's alternative ruling under the rule of reason was predetermined by its (erroneous) *per se* ruling. Thus the district court assessed [5] impacts on competition without recognizing that Apple's role as a vertical player differentiated it from the publishers. The court should instead have considered Apple as a competitor on the distinct horizontal plane of retailers, where Apple competed with Amazon (and smaller players such as Barnes & Noble). **(POINT II)**

- Apple's conduct, assessed under the rule of reason on the horizontal plane of retail competition, was unambiguously and overwhelmingly procompetitive. Apple was a major potential competitor in a market dominated by a 90 percent monopoly, and was justifiably unwilling to enter a market on terms that would assure a loss on sales or exact a toll on its reputation. In that connection, the district court erroneously deemed the monopolist's $9.99 price as categorically good for competition because it was lower than cost, and because e-book prices rose after the monopoly was broken. **(POINT III)**

A further and pervasive error (by the district court and by my colleagues on this appeal) is the implicit assumption that competition should be genteel, lawyer designed, and fair under sporting rules, and that antitrust law is offended by gloves-off competition.

[6]

BACKGROUND

From the 2007 inception of the U.S. retail market for e-books through 2009, Amazon "dominated the e-book retail market, selling nearly 90% of all e-books." *Apple I*, 952 F. Supp. 2d at 649. It assured its domination by charging its retail customers $9.99 for new releases and bestsellers, below the wholesale price that Amazon was paying to publishers. *Id.* at 649-50, 708. The popular media reported that Amazon "takes a loss on the sale of the most popular e-books." *Id.* at 652. That pricing deterred potential retail competitors from entering the relevant market—"trade e-books in the United States"[1]—because an entrant "would run the risk of losing money if it tried or was forced to match Amazon's pricing to remain competitive." *Id.* at 658.

Amazon's below-cost pricing was also a threat to publishers, because at a $9.99 price point, e-books cannibalized sales of (more profitable) hardcover editions. *Id.* at 649. Although the major publishers believed Amazon's below cost pricing was "predatory," *id.* at 653, each publisher understood that it was powerless to

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[1] The parties did not dispute this market definition. *Apple I*, 952 F. Supp.2d at 694 n.60.

take on Amazon, *id*. at 650. Publishers feared that Amazon might [7] "compete directly with publishers by negotiating directly with authors and literary agents for rights," *id*. at 649, and might "retaliate" against insubordinate publishers "by removing the 'buy buttons' on the Amazon site that allow customers to purchase books … or by eliminating [a publisher's] products from its site altogether," *id*. at 679. One publisher, Macmillan, suffered such retaliation when Amazon removed the "buy buttons" for print and e-book versions of Macmillan titles. *Id*.

Amazon's 90 percent market share constituted a monopoly under antitrust law. *See, e.g.*, *Am. Tobacco Co. v. United States*, 328 U.S. 781, 797 (1946) (characterizing as "a substantial monopoly" a market share of "over 80% of the field"); 3B Areeda & Hovenkamp, Antitrust Law ¶ 801 (3d ed. 2008). Amazon's below-cost pricing was a barrier to entry by Apple in 2009, when it contemplated entry into the e-book retail market via the iPad.[2] *Apple I*, 952 F. Supp. 2d at 654, [8] 658. Ap-

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[2] While the district court did not use the label "barrier to entry," its findings of fact made the point clearly. In finding that a new entrant to e-book retail in 2009 "would run the risk of losing money if it tried or was forced to match Amazon's pricing to remain competitive," Apple I, 952 F. Supp. 2d at 658, the district court left no doubt that the effect of Amazon's below-cost pricing regime was to "impede entry and protect existing market power"—the basic operation of a barrier to entry, 2B Areeda & Hovenkamp, supra, ¶ 420c, at 78.

The majority disputes whether there was any barrier to entry under Amazon's below-cost pricing regime, because at least one competitor attempted to join the market. See Op. of Judge Livingston, ante, at 13 (for the Court), 100. Even if that entrant had any chance of success (nobody contends that it sold a meaningful number of e-books, or made any money, or reduced Amazon's mammoth market share to less than 90 percent), that fact need not ple nevertheless undertook to develop an e-book retail platform in time for the iPad's launch, scheduled for January 27, 2010. *Id.* at 654-55. However, "Apple did not have to open an e-bookstore when it launched the iPad"; and it was willing to enter the market only on the condition that its e-book retail business would be profitable, such that Apple could "compete effectively with Amazon" without adopting a loss-leadership and below-cost pricing strategy. *Id.* at 656-59.

Apple opened extensive negotiations with publishers to determine how if at all it could enter the e-book retail market. *Id.* at 655-57. Apple met with the leaders of the six largest publishing houses in the United States: Hachette, HarperCollins, Macmillan, Penguin, Random House, and Simon & Schuster. *Id.* at 647, 655. At the outset, Apple understood that the publishers were unhappy with Amazon's below-cost pricing of e-books; so Apple knew that the publishers [9] "were willing to coordinate their efforts" to combat the $9.99 price point. *Id.* at 656.

After some weeks, Apple and several publishers devised a new model for e-book distribution. Amazon had been paying a wholesale price for each e-book, and reselling (often at a loss) for a retail price of its choosing. Apple's distribution contracts would adopt an agency system: publishers would set the retail prices of e-books sold through Apple's platform and Apple would take a fixed-percent commission on each sale. *Id.* at 659. However, the agency model would expose Apple (or any retailer) to risk, because publishers might protect hardcover sales by setting retail prices for e-

imply ease of entry because "a barrier may protect a market incumbent without completely excluding entry." 2B Areeda & Hovenkamp, supra, ¶ 420a, at 73.

books so high that Apple would appear out of touch with consumers aware of Amazon's $9.99 price. *Id.* Apple's solution was twofold. First, the proposed agency contract included a most favored nation ("MFN") clause, under which publishers must price their new releases in Apple's store at or below the lowest price offered by any other e-book retailer. *Id.* at 662. The district court found that the MFN clause "effectively forced" each publisher that signed Apple's agency contract to move its other retailers onto the agency model. *Id.* at 664. That is because, once Apple's cost was set as a percentage of the retail price, the publishers would suffer if Apple **[10]** matched Amazon's $9.99 retail price. Second, the proposed contract included maximum prices for various categories of e-books. *Id.* at 661-62. The district court found that these tiered price caps had the effect of setting anchor prices across the e-book industry. *Id.* at 670. Nonetheless, as the district court observed, these terms are not inherently illegal, and "entirely lawful contracts may include an MFN, price caps, or pricing tiers." *Id.* at 698.

As Apple negotiated with publishers to sign the agency contract, it told each major publisher that all signing publishers would receive the same terms. *Id.* at 667. In the end, five of the six largest publishers signed Apple's agency contract. *Id.* at 673. (Only Random House, the country's largest, did not. *Id.*) As the district court found, the five signatories represented "over 48% of all e-books in the United States" when they signed Apple's agency contract. *Id.* at 648. Apple unveiled its e-book retail platform—the "iBookstore"—at the first public demonstration of the iPad on January 27, 2010. *Id.* at 678-79.

After the publishers signed on to Apple's agency contract, they had to focus on Amazon's adoption of the agency model because otherwise (as explained above) the MFN clause would allow Apple to match Amazon's price for bestsellers, and pay the publishers no more than a percentage commission on **[11]** $9.99. However, "the [p]ublishers feared retaliation from Amazon unless they acted in unison," *id.* at 670, and "needed reassurance that they would not be alone," *id.* at 674. An Apple executive liaised with each of the five signatory publishers, to encourage a "united front" in their negotiations with Amazon, and to keep the publishers "apprised about who was in and how many were on board." *Id.* at 673. The publishers also communicated directly with each other. *Id.* at 674-77. When Amazon realized that the five publishers were acting in concert, it acceded and signed the agency contracts. *Id.* at 680-82.

Those are the findings on which Apple was adjudged to have committed an antitrust violation. The putative violation amounted to: (a) embedding the agency model (complete with MFN clauses and price caps) in Apple's own contracts with publishers and (b) encouraging the publishers to coordinate horizontally in their efforts to push the industry-wide adoption of the agency model. Apple and the publishers shared the motive to increase the publishers' pricing power in order to deprive Amazon of its monopoly. They succeeded: as the district court noted earlier in this litigation, "Amazon's market share in ebooks decreased from 90 to 60 percent in the two years following the **[12]** introduction of agency pricing." *United States v. Apple, Inc.*, 889 F. Supp. 2d 623, 640 (S.D.N.Y. 2012).

* * *

The foregoing Background accepts and relies upon the district court's findings of fact. One cannot say the same of Judge Livingston's opinion, which supports its legal conclusions and its market analysis with novel findings made now on appeal, i.e., remand by other means. A few examples:

- The notion that Amazon's below-cost pricing was loss-leadership "designed to encourage consumers to adopt the Kindle," Op. of Judge Livingston, ante, at 13 (for the Court), is a novelty, supported by neither the fact findings nor the record. At any rate, the effect of e-book pricing outside of the relevant market is irrelevant.

- The majority asserts that Amazon's below-cost pricing was limited to only "a small loss" on only "a small percentage of its sales." *Id.* at 85 (for the Court). These observations are apparently drawn from a submission by Amazon, downplaying the anti-competitive effects of its monopoly-protective pricing. The district court did not rely on these statistics, presumably because they are misleading and self-serving: they ignore that **[13]** the minority of titles comprising new releases and bestsellers naturally have an outsize impact on the industry. Accordingly, the district court found that the below-cost pricing had consequences on the market, namely that a new entrant "would run the risk of losing money if it tried or was forced to match Amazon's pricing to remain competitive." Apple I, 952 F. Supp. 2d at 658.

- I can find no record support for the narrative that Amazon's market share was eroding before Apple's entry, that the iPad "promised to introduce more competition with or without Apple's iBookstore," and that the publishers

> thereby enjoyed increased negotiating leverage. Op. of Judge Livingston, ante, at 103-04. Similarly, the assertion that Barnes & Noble disrupted Amazon's dominance in the e-book market, *see id.* at 103, is supported neither by the district court's findings nor by the record.

By contrast, my antitrust analysis relies on the findings made by the district court, and incorporates no others, in order (a) to avoid factual disputes with my colleagues, (b) to defer to the district court's thorough fact findings in **[14]** arriving at my legal conclusions, and (c) to respect the limited role of appellate courts.

DISCUSSION

I

The district court's principal legal error, from which other errors flow, is its conclusion that Apple violated § 1 under the *per se* rule. Having found that the publishers' coordinated strategy was a horizontal price-fixing conspiracy, and that Apple had facilitated that conspiracy in its vertical relationship with the publishers, *see Apple I*, 952 F. Supp. 2d at 691, the district court drew the legal conclusion that these facts established a *per se* violation of the Sherman Act by Apple. This appeal turns on whether purely vertical participation in and facilitation of a horizontal price-fixing conspiracy gives rise to *per se* liability.

Section 1 of the Sherman Act "outlaw[s] only *unreasonable* restraints"; so a court weighing an alleged violation "presumptively applies rule of reason analysis, under which antitrust plaintiffs must demonstrate that a particular contract or combination is in fact unreasonable and anticompetitive before it will be found unlawful." *Texaco Inc. v. Dagher*, 547 U.S. 1, 5 (2006) (quoting *State Oil* **[15]** *Co. v. Khan*, 522 U.S. 3, 10 (1997)). The exception, liability *per se*, is reserved for those categories of behavior so definitively and universally anti-competitive that a court's consideration of market forces and reasonableness would be pointless. *Id.* Traditionally, restraints that are *per se* unlawful take the form of horizontal agreements "raising, depressing, fixing, pegging, or stabilizing the price of a commodity." *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 223 (1940).

Among modern cases, the *per se* rule takes aim exclusively at *horizontal* agreements, because "competition among the manufacturers of the same [product] … is the primary concern of antitrust law." *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 52 n.19 (1977). Accordingly, the trend of antitrust law has been a steady constriction of the *per se* rule in the context of vertical relationships. *See, e.g.*, *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 901 (2007) (holding that vertical agreements for minimum prices are not *per se* violations); *State Oil Co.*, 522 U.S. at 7 (holding that vertical agreements for maximum prices are not *per se* violations); *Continental T.V.*, 433 U.S. at 59 (holding that vertical non-price restraints are not *per se* violations); *White Motor Co. v. United States*, 372 U.S. 253, 261-64 (1963) (holding that vertical territorial **[16]** restraints are not *per se* violations). The cases have "continued to temper, limit, or overrule once strict prohibitions on vertical restraints." *Leegin*, 551 U.S. at 901.

A vertical relationship that facilitates a horizontal price conspiracy does not amount to a *per se* violation. In another age, the Supreme Court treated such a hub-and-spokes conspiracy as a *per se* violation. *See Interstate Circuit, Inc. v. Paramount Pictures Distrib. Co.*, 306 U.S. 208, 226-27 (1939). But the *per se* rule has been in steady retreat.

The most recent and explicit signal is given in *Leegin*, which explains that "the Sherman Act's prohibition on 'restraints of trade' evolves to meet the dynamics of present economic conditions," such that "the boundaries of the doctrine of *per se* illegality should not be immovable." 551 U.S. at 899-900 (alterations omitted). *Leegin* held that a manufacturer did not commit a *per se* violation of § 1 when it agreed with several retailers on a minimum price that the retailers could charge—a holding that overruled a century-old principle articulated in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911). *See Leegin*, 551 U.S. at 881. *Leegin* reasoned that *Dr. Miles* had "treated vertical agreements a manufacturer makes with its distributors as analogous to a horizontal combination among competing distributors," but that, "[i]n later cases, **[17]** … the Court rejected the approach of reliance on rules governing horizontal restraints when defining rules applicable to vertical ones." *Leegin*, 551 U.S. at 888. *Dr. Miles* was held to be inconsistent with "[o]ur recent cases[,] [which] formulate antitrust principles in accordance with the appreciated differences in economic effect between vertical and horizontal agreements, differences the *Dr. Miles* Court failed to consider." *Id.*

Although the express holding of *Leegin* does not extend beyond the overruling of *Dr. Miles*, the Court's analysis reinforces the doctrinal shift that subjects an ever-broader category of vertical agreements to review under the rule of reason. The Court first stated the subsisting scope of *per se* liability:

> A horizontal cartel among competing manufacturers or competing retailers that decreas-

> es output or reduces competition in order to increase price is, and ought to be, *per se* unlawful.

Leegin, 551 U.S. at 893. The Court then rejected *per se* liability for hub-and-spokes agreements, in wording that prescribes rule-of-reason review of vertical dealings that facilitate *per se* unlawful horizontal agreements (the type of agreement that the district court found Apple had undertaken):

> To the extent a vertical agreement setting minimum resale prices is entered upon to *facilitate* either type of cartel [among **[18]** manufacturers or among retailers], it, too, *would need to be held unlawful under the rule of reason.*

Id. (emphasis added). After *Leegin*, we cannot apply the *per se* rule to a vertical facilitator of a horizontal price-fixing conspiracy; such an actor must be held liable, if at all, "under the rule of reason." *Id.*

Leegin is animated by the "appreciated differences in economic effect between vertical and horizontal agreements." *Id.* at 888. Since every challenged restraint is thus classified as either horizontal or vertical, one may draw certain reliable inferences: vertical agreements are not presumptively subject to *per se* liability; the vertical nature of the agreement is its salient feature; the influence of a vertical arrangement on a horizontal cartel (on another plane of competition) does not render the vertical arrangement *per se* unlawful.

Our only sister circuit to have considered this wording from *Leegin* arrived at the conclusion I draw. In *Toledo Mack Sales & Service, Inc. v. Mack Trucks, Inc.*, 530 F.3d 204, 225 (3d Cir. 2008), a manufacturer used its contracts with distributors to facilitate and enforce a horizontal conspiracy (among the distributors) that was itself illegal *per se*. *See id*. at 210. The Third Circuit held that *Leegin*'s instruction—that the vertical arrangement "would need to be held [19] unlawful under the rule of reason"—prescribed the rule of reason as the proper analysis for whether the vertical conduct violated § 1. *See id*. at 225.

Taking the opposite tack, the majority opinion on this appeal insists that a vertical facilitator of a horizontal conspiracy is liable *per se*, even after *Leegin*. In support of that argument, the majority cites seven cases that pre-date *Leegin*.[3] Op. of Judge Livingston, ante, at 73-77 (for the Court). The majority cites only one post-*Leegin* case that considers this question: namely, the Third Circuit's analysis of a conspiracy that involved both vertical *and* horizontal relationships, concluding that the horizontal relationships violated § 1 *per se* and that pursuant [20] to *Leegin* the vertical rela-

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[3] The cases are cited by the majority in this order: *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959); *United States v. General Motors Corp.*, 384 U.S. 127 (1966); *Toys "R" Us, Inc. v. FTC*, 221 F.3d 928 (7th Cir. 2000); *Denny's Marina, Inc. v. Renfro Productions, Inc.*, 8 F.3d 1217 (7th Cir. 1993); *United States v. MMR Corp.*, 907 F.2d 489 (5th Cir. 1990); *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717 (1988); *NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128 (1998).

Just as unhelpfully, the majority cites dicta from a Sixth Circuit case affirming the dismissal of a lawsuit that alleged a hub-and-spokes conspiracy. *See Total Benefits Planning Agency, Inc. v. Anthem Blue Cross & Blue Shield*, 552 F.3d 430 (6th Cir. 2008). The majority cites the case as if its holding supports the continued legitimacy of the hub-and-spokes theory after *Leegin*, a flawed interpretation given the Sixth Circuit's disposition on the hub-and-spokes claim. *Id.* at 435 (holding that plaintiffs inadequately alleged a *horizontal* conspiracy and that, after *Leegin*, "all *vertical* price restraints are to be judged under the rule-of-reason standard" (emphasis added)).

tionships "would have to be analyzed under the traditional rule of reason."[4] *In re Ins. Brokerage Antitrust Litig.*, 618 F.3d 300, 318 (3d Cir. 2010).

The majority's holding in this case therefore creates a circuit split, and puts us on the wrong side of it.

"[H]orizontal agreements *as a class* deserve stricter scrutiny than … vertical agreements," because horizontal agreements "pose the most significant dangers of competitive harm." 11 Areeda & Hovenkamp, *supra*, ¶ 1902a, at 232. Horizontal price conspiracies are illegal *per se* because motives of horizontal **[21]** players are aligned and dominant and create irresistible temptations. *See, e.g.*, Adam Smith, *The Wealth of Nations* 207 (Collier 1902) (1776) ("People of the same trade seldom meet together … , but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices.").

Collusion among competitors does not describe Apple's conduct or account for its motive. Apple's conduct had no element of collusion with a horizontal rival. Its

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[4] The Third Circuit analyzed a network of restraints, including a conspiracy among insurance brokers, a conspiracy among insurers, and agreements that connected the brokers and insurers. The court explained *Leegin*'s impact this way:

> Under the Supreme Court's jurisprudence, virtually all vertical agreements now receive a traditional rule-of-reason analysis. *See Leegin*, 551 U.S. 877. In the factual context of this case, a horizontal agreement means … an agreement among either the brokers or the insurers in the global conspiracy. Agreements between brokers and insurers, on the other hand, are vertical and would have to be analyzed under the traditional rule of reason.

In re Ins. Brokerage Antitrust Litig., 618 F.3d 300, 318-19 (3d Cir. 2010) (internal citation and footnote omitted).

own rival in competition was (and presumably is) Amazon; and that competition takes place on a horizontal plane distinct from the plane of the horizontal conspiracy among the publishers. All Apple's energy—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. On the only horizontal plane that matters to Apple's e-book business, Apple was in competition and never in collusion. So it does not do to deem Apple's conduct anti-competitive just because the publishers' horizontal conspiracy was found to be illegal *per se*.

"[V]ertical agreements are a customary and even indispensable part of the market system" and so do not represent the same presumptive threat to competition. 11 Areeda & Hovenkamp, *supra*, ¶ 1902d, at 240. Even a vertical **[22]** agreement designed to decrease competition among competitors does not pose the threat to market competition that is posed by a horizontal agreement, for two reasons: (1) market forces (such as countervailing measures by competitors) are categorically more effective in countering anti-competitive vertical agreements, and (2) vertical agreements are so fundamental to the operation of the market that uncertainty about the legality of vertical arrangements would impose vast costs on markets. *Id.* at 240-41. Such market realities are driving the evolution of antitrust law, which has "rejected the approach of reliance on rules governing horizontal restraints when defining rules applicable to vertical ones." *Leegin*, 551 U.S. at 888.

The present case illustrates why *per se* treatment is not given to vertical agreements that facilitate horizontal conspiracies. Assuming (as is uncontested on appeal) that the publishers violated § 1 *per se* through their coordination, Apple's promotion of that horizontal conspiracy was limited to vertical dealings.

The *per se* rule is inapplicable here for another independent reason: The *per se* rule does not apply to arrangements with which the courts are not already well-experienced. *Leegin*, 551 U.S. at 887. As the government conceded at oral argument, no court has previously considered a restraint of this kind. Several [23] features make it *sui generis*: (a) a vertical relationship (b) facilitating a horizontal conspiracy (c) to overcome barriers to entry in a market dominated by a single firm (d) in an industry created by an emergent technology.

As I undertake to show in my analysis under the rule of reason, below, the restrictive market conditions Apple faced and the pro-competitive results of Apple's conduct make its vertical dealings categorically reasonable. Even if one tests that conclusion under the rule of reason, the analysis is sufficiently complex and yields such substantial pro-competitive results that *per se* liability is an abdication of the duty to distinguish reasonable restraints from those that are unreasonable.

II

Having concluded first that Apple's conduct was anti-competitive *per se*, corollary errors followed when the district court turned to the rule of reason. Once a court finds that a party acted unreasonably *per se* in a set of transactions, an epiphany is required for the court to conclude that the same party acted reasonably doing the same acts in the same role at the same time. The influence arising from the district court's *per se* accusation of wrongdoing infected all [24] analysis that followed. Once Apple was deemed to have joined a conspiracy that was illegal *per se*, its goal, motive, and conduct seemingly needed (and got) no additional scrutiny—legal or moral or economic.

Having confirmed Apple's *per se* liability by conflating the horizontal plane of competition among publishers with the horizontal plane of competition among retailers, the district court committed the same error in its rule of reason analysis. Thus the district court (as explained below) overstated the anti-competitive nature of Apple's vertical dealings and overlooked the pro-competitive effects on retail competition—the horizontal plane on which Apple does e-book business. "The district court did not analyze the state of competition between ebook retailers," as the majority concedes. Op. of Judge Livingston, ante, at 44 (for the Court) (emphasis omitted). Exactly.

Judge Livingston's opinion succumbs to the same fallacy by declaring the majority's own *per se* analysis so overwhelming that full rule-of-reason scrutiny requires no more than a "quick look." Quick-look analysis is an appropriate tool only when "an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect." *Cal. Dental Ass'n v. FTC*, 526 U.S. 756, 770 (1999). Quick-look analysis is [25] not a tool for cutting corners. Judge Livingston's opinion justifies quick-look analysis by referring to e-book price increases that form the majority's earlier argument for the application of the *per se* rule, *see* Op. of Judge Livingston, ante, at 93—price increases that, at any rate, are the expected result when monopolistic below-cost pricing dissipates.

In form and substance, Judge Livingston's analysis demonstrates that when one starts with a finding of unreasonableness *per se*, the rule of reason analysis is tainted. It is called confirmation bias. The characterization of Apple's conduct as "vigilantism" is telling. Op. of Judge Livingston, ante, at 9 (for the Court), 98. Use of that word either assumes the conclusion that the conduct is illegal, or else confuses it with self-help (which used to be a virtue).

III

On this appeal, we have reached no majority as to the rule of reason. Judge Livingston writes for herself alone that, as an alternative to the *per se* rule, she would also affirm under the rule of reason; without a second judge supporting this conclusion, it is dicta, because our affirmance is based on the *per se* theory adopted by two judges. Unlike my colleagues, I must address the rule of reason, **[145]** because my vote to reverse depends on my conclusion that this alternative theory of liability is every bit as untenable as liability *per se*.

Analysis under the rule of reason—whether conducted in full or by an *untainted* quick look—compels the conclusion that Apple did not violate § 1 of the Sherman Act. The issue is decided by comparing (a) the restrictive effect of Apple's dealings with (b) the pro-competitive result of deconcentrating a market that had been dominated by a monopolist and insulated from competition through below-cost pricing.

Under the rule of reason, the initial burden rests with the plaintiffs "to demonstrate the defendants' challenged behavior had an *actual* adverse effect on competition as a whole in the relevant market." *Geneva Pharms. Tech. Corp. v. Barr Labs. Inc.*, 386 F.3d 485, 506-07 (2d Cir. 2004) (internal quotation marks omitted). Upon plaintiffs' showing of such an effect, "the burden shifts to the defendants to offer evidence of the pro-competitive effects of their agreement," and then "the burden shifts back to the plaintiffs to prove that any legitimate competitive benefits offered by defendants could have been achieved through less restrictive means." *Id.* The reasonableness of the restraint then boils down [27] to whether the dominant effect of the agreement is to promote competition or restrain it. *Id.*

Analysis begins with an accounting of anti-competitive effects. Apple's vertical conduct consisted of negotiating the terms of its own contracts. Of course, every contract is a restraint of trade to some extent, *see Nat'l Collegiate Athletic Ass'n v. Bd. of Regents of Univ. of Okla.*, 468 U.S. 85, 98 (1984); so this fact alone is neither here nor there.

The agency agreement that Apple signed with each publisher was innocuous: as the parties agree, each term—including the agency structure, MFN clause, and price caps—is absolutely legal. The district court so found expressly:

> The Plaintiffs do not argue, and this Court has not found, that the agency model for distribution of content, or any one of the clauses included in the Agreements, or any of the identified negotiation tactics is inherently illegal. Indeed, entirely lawful contracts may include an MFN, price caps, or pricing tiers.

Apple I, 952 F. Supp. 2d at 698. The main restraint resulting from Apple's vertical conduct was the shifting of pricing power from e-book retailers to e-book publishers. And this effect operated as a restraint only in the sense that Amazon faced pressure to adopt an agency model and to charge prices set by the five [28] publishers, which of course remained in competition with each other, and with the publishers who account for the remaining 52 percent of the industry.

The district court opinion and the plaintiffs' briefs fixate on the idea that Apple ended Amazon's $9.99 price for most new releases and bestsellers, and that consumers would have preferred a lower price. But the consumer's near term preference for low prices is not an object of antitrust law. *See Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 237 (1993). The district court charts the short-term price developments, treating the end of below-cost pricing as anti-competitive and observing with disapproval the natural tendency for prices to rise to competitive levels. The rule of reason promotes competition; it can be safely assumed that if competition sharpens, prices will take care of themselves.

As to the pro-competitive effects, the rule of reason must take account primarily of the deconcentrating of the e-book retail market. The benefit of increasing the number of firms in a market derives from the "inverse correlation between concentration and competition." Eleanor M. Fox, Economic Concentration, Efficiencies and Competition: Social Goals and Political Choices, *in* Industrial Concentration and the Market System 137, 149 (Eleanor M. Fox & **[29]** James T. Halverson eds., 1979). As the district court found, Apple was weighing its entry into the retail e-book market, and the agency structure was the only way Apple would enter the market. Nobody has proposed—before *or* since Apple's entry—any "less restrictive means" by which Apple could have achieved the same competitive benefits. See Geneva Pharms., 386 F.3d at 507 (plaintiffs' burden to prove viable and less restrictive alternative). Apple's challenged conduct broke Amazon's monopoly, immediately deconcentrated the e-book retail market, added a platform for reading e-books, and removed barriers to entry by others. And removal of a barrier to entry reduces for the long term a market's vulnerability to monopolization.[5] These effects sound in the basic goals of antitrust law. Even if only quick-look analysis were appropriate in this case, these effects would vindicate Apple's conduct. (Judge Livingston's opinion discounts this pro-competitive effect by noting the open question whether "below-cost pricing is unlawfully anti-competitive," thereby suggesting that **[30]** Apple's dismantling of the entry barrier could be pro-competitive only if the barrier was itself a Sherman Act violation. Op. of Judge Livingston, ante, at 97. But it is no matter whether the insuperable barrier that Apple tore down had been raised lawfully or not.)

Another pro-competitive effect is the encouragement of innovation, a hallmark and benefit of competition. Apple began retailing e-books in conjunction with its release of the iPad, a device that integrated cutting-edge functions and applications, just one of which was the capacity for users to buy and read e-books. It is impossible to know the likely course of innovation, and pro-competitive effects of innovation cannot be measured; nevertheless, the encouragement of innovation must be afforded considerable weight under the rule of reason. *See generally* 2B Areeda & Hovenkamp, *supra*, ¶ 407. Apple's business is not the technology of the clothespin.

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[5] Generally speaking, entry barriers permit monopolization and monopoly power allows a firm to erect entry barriers. *See, e.g., Port Dock & Stone Corp. v. Oldcastle Ne., Inc.*, 507 F.3d 117, 125 (2d Cir. 2007); *United States v. Microsoft Corp.*, 253 F.3d 34, 82 (D.C. Cir. 2001) (en banc); *see also Mobil Oil Corp. v. Fed. Power Comm'n*, 417 U.S. 283, 302 n.23 (1974). Each is less likely to arise when the other is absent from a market.

The restraint of Apple's vertical conduct was no more than a slight offset to the competitive benefits that now pervade the relevant market.[6]

[31] How else could the competitive benefits have been realized in this market? In the course of this litigation, three theories have been offered for how Apple could have entered the e-book market on less restrictive terms. Each theory misapprehends the market or the law, or both. The absence of alternative means bespeaks the reasonableness of the measures Apple took.

Theory 1: Apple could have competed with Amazon on Amazon's terms, using wholesale contracts and below-cost pricing. This was never an option. The district court found as fact that: a new entrant into the e-book retail market "would run the risk of losing money if it tried or was forced to match Amazon's pricing to remain competitive," *Apple I*, 952 F. Supp. 2d at 658; Apple was "not willing" to engage in below-cost pricing, *id.* at 657; and Apple could have avoided this money-losing price structure simply by forgoing entry to the market, *see id.* at 659. Even if Apple had been willing to adopt below-cost pricing, the result at best would have been duopoly, and the hardening of the existing barrier to entry. Antitrust law disfavors a durable duopoly nearly as much as monopoly itself. *See* 6 Areeda & Hovenkamp, *supra*, ¶ 1429.

Theory 2: Apple could have entered the e-book retail market using the wholesale model and charged higher prices than Amazon's. The district court fore-

[6] Amazons's below-cost prices also threatened the market for hard-copy books, *see Apple I*, 952 F. Supp. 2d at 649, and thus the royalties of authors, who may well consider that they have some role in this industry.

closed this **[32]** theory as well; it found that Apple refused to impair its brand by charging "what it considered unrealistically high prices." Apple I, 952 F. Supp. 2d at 659. Even if Apple had been willing to tarnish its brand by offering bad value for money, the notion that customers would actually have bought e-books from Apple at the higher price defies the law of demand. Higher prices may stimulate sales of certain wines and perfumes—not e-books.[7]

Nor could Apple justify higher prices for the e-books by competing on the basis of its new hardware, the iPad, because there is inter-operability among platforms. And if Apple had attempted to pursue this hardware-based competition by programming its iPad to run the iBookstore but to reject Amazon's Kindle application, Apple might have been exposed to an entirely different antitrust peril. *See United States v. Microsoft Corp.*, 253 F.3d 34, 50-80 (D.C. Cir. 2001) (en banc); *Google Android*, No. 40099 (Eur. Comm'n Apr. 15, 2015) (antitrust proceedings brought by European Commissioner for **[33]** Competition against Google for favoring Google's own applications on mobile devices that use Google's operating system).

Theory 3: Apple could have asked the Department of Justice to act against Amazon's monopoly. Counsel for the United States actually proposed this at oral ar-

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[7] In economic terms, e-books are subject to the law of demand and therefore have negative price elasticity of demand. *See generally* N. Gregory Mankiw, Principles of Economics 67 (6th ed. 2012). E-books are neither Veblen goods nor Giffen goods, nor do they have perfectly inelastic demand. *See id.* at 92-93, 453-54, 835; Laurie Simon Bagwell & B. Douglas Bernheim, Veblen Effects in a Theory of Conspicuous Consumption, 86 Am. Econ. Rev. 349 (1996).

gument. At the same time, however, he conceded that the Department of Justice had already "noticed" Amazon's e-book pricing and had chosen not to challenge it because the government "regarded it as good for consumers." Any request from Apple would therefore have been futile. True, Apple could not have known that the Antitrust Division would have adopted the position that below-cost pricing is not a concern of antitrust policy: who could have guessed that the government would adopt a policy that is primitive as a matter of antitrust doctrine and illiterate as a matter of economics? Nevertheless, hindsight reveals that government antitrust enforcement against Amazon was not an option.

More fundamentally, litigation is not a *market* alternative. This observation has especial force in markets that are undergoing rapid technological advance, where the competitive half-life of a product is considerably more brief than the span of antitrust litigation. A requirement that potential market entrants litigate **[34]** instead of enter the market on restrictive (but legal and reasonable) terms, would license monopoly for the duration.

* * *

Apple took steps to compete with a monopolist and open the market to more entrants, generating only minor competitive restraints in the process. Its conduct was eminently reasonable; no one has suggested a viable alternative. "What could be more perverse than an antitrust doctrine that discouraged new entry into highly concentrated markets?" In re Text Messaging Antitrust Litig., 782 F.3d 867, 874 (7th Cir. 2015).

Application of the rule of reason easily absolves Apple of antitrust liability. That is why at oral argument the government analogized this case to a drug conspiracy, in which every player is a criminal—at every level, on every axis, whether big or small, whether new entrant or recidivist. The government found the analogy useful—and necessary—because in an all-criminal industry there is no justification or harbor under a rule of reason.

[154]

IV

Because I see no antitrust violation, I need not consider Apple's separate challenge to the injunction itself. My colleagues, for their own good reasons, do not reach that challenge either. Yet the injunction and its shortcomings bear upon the institutional interest of the courts; and Apple's challenge deserves some response. In my view, the injunction warps the role of a neutral, court-appointed referee into that of an adversary party, with predictable consequences.

The monitor is an arm of the district court, and owes loyalty in that direction only. *See* Fed. R. Civ. P. 53(a). But the injunction redirects the loyalty of the monitor to Apple's chief adversary in the litigation, the Department of Justice. Under the injunction, the DOJ recommends the monitor (Injunction ¶ VI(A)), approves the monitor's fees (*id.* ¶ VI(I)), and mediates disputes between the monitor and Apple (*id.* ¶¶ VI(E), (H)). Thus the injunction first creates a neutral fact-finding office, and then gives an adversary the ability to decide who holds the office, how much he gets paid (out of the other side's pocket), and how broadly he may reach and inquire. Reciprocally, the monitor is directed to inform the government if he "discovers or receives evidence that suggests" further antitrust violations, whether or not related to this litigation. **[36]** (*Id.* ¶ VI(F).) This is a device that must misfire.

As events have happened (and were seemingly fore-ordained) the monitor has reason to look to the DOJ with gratitude and loyalty. The DOJ recommended Michael Bromwich as monitor, and the district court appointed him. *United States v. Apple Inc.*, --- F.3d ----, 2015 WL 3405534, at *2 (2d Cir. May 28, 2015). Without a meaningful cap on his fee, Bromwich proposed that defendant Apple compensate him at $1,265 per hour—an eye-popping rate for service as an agent of a court. *Id.* at *3. (Because Bromwich lacks antitrust expertise, he proposed to add an actual antitrust lawyer to the team at $1,025 an hour. *Id.*) When Apple challenged that tariff as unreasonable, Bromwich explained that the injunction gave Apple no standing to object: "the fees and expenses to be paid to the monitor and his team are not set by Apple; they are set by the monitor, with approval reserved for the DOJ and the Plaintiff States." *Id.* (quoting Bromwich). Bromwich was right, which is telling: the injunction contemplated no role for the judge.

Once the Department of Justice selected him and approved his hourly fee, Bromwich drew up his own mandate. Although the injunction contemplated that the monitor would check sufficiency of an antitrust policy that Apple was to **[37]** prepare in 90 days (and Apple's compliance with it), Bromwich started his inquiry immediately on his appointment; he multiplied interviews, document inspections, and discontents; he demanded to interview Apple executives without the presence of Apple's chosen counsel; and he took aim at the competitive culture of the corporation generally—a culture that is obviously aggressive, but just as obviously no business of the courts. *See id.* at *2-3, *7.

Having thus been selected by an adversary party, paid at a rate approved by the adversary party, and directed to look to the adversary party for the mediation of disputes, Bromwich was (in every respect important to a lawyer) retained and run by the adversary. Apple had an unenviable choice: it could accept scrutiny by a lawyer whose incentives were corrupted by the injunction that created his office, or attack the fee and the widening scope of inquiry, thereby sharpening the confrontations created by the mechanics of the injunction.

A magistrate judge has cut Bromwich's hourly fee. *Id.* at *6 n.4. And a panel of this Court has construed narrowly the scope of the monitor's inquiries. *Id.* at *4. But the structural defect of the injunction remains: allowing an arm of the court to serve as agent of an adversary party. It would take strong stuff for a lawyer to transcend the worldly incentives of this injunction: unlimited work at [38] the (now cut) rate of $1,000 an hour, paid by a solvent party that may expect retaliation for protesting, in order to perform a monitorship subject to extension by the court for reasons that will be influenced by input from the monitor himself.

An injunction that thus blurs the lines of the adversary system does no good for the reputation of the courts.

APPENDIX B

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Nos. 12-cv-2826 (DLC), 12-cv-399 (DLC)

UNITED STATES OF AMERICA,
Plaintiff,
v.
APPLE, INC., *et al.*,
Defendants,

THE STATE OF TEXAS, *et al.*,
Plaintiffs,
v.
PENGUIN GROUP (USA) INC., *et al.*,
Defendants,

* * *

DENISE COTE, District Judge:*

This Opinion explains how and why the prices for many electronic books, or "e-books," rose significantly in the United States in April 2010. Plaintiffs the United States of America ("DOJ") and thirty-three states and U.S. territories (the "States") (collectively, "Plaintiffs"), filed these antitrust suits on April 11, 2012, alleging that defendant Apple Inc. ("Apple") and five book publishing companies conspired to raise, fix, and stabilize the retail

* Table of contents from original document omitted.

price for newly released and bestselling trade e-books in violation of Section 1 of the Sherman Antitrust Act, 15 U.S.C. § 1 ("Sherman Act"), and various state laws. These cases represent two of four related actions brought before this Court alleging the same e-books price-fixing conspiracy between Apple and the publishers.[1] The publishers are Hachette Book Group, Inc. ("Hachette"), HarperCollins Publishers LLC ("HarperCollins"), Holtzbrinck Publishers LLC d/b/a Macmillan ("Macmillan"), Penguin Group (USA), Inc. ("Penguin"), and Simon & Schuster, Inc. ("Simon & Schuster" or "S&S") (collectively, "Publisher Defendants").

Only Apple proceeded to trial; the Publisher Defendants have settled their claims with both the DOJ and the States. This Opinion presents the Court's findings of fact and conclusions of law following the bench trial that was held from June 3 to 20, 2013 to resolve the issue of Apple's liability and the scope of any injunctive relief. As described below, the Plaintiffs have shown that Apple conspired to raise the retail price of e-books and that they are entitled to injunctive relief. A trial on damages will follow.

PROCEDURAL HISTORY

Fact and expert discovery in these actions concluded on March 22, 2013. The parties' Joint Pretrial Order,

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[1] The other two cases are *State of Texas, et al. v. Hachette Book Group, Inc., et al.*, 12 Civ. 6625 (DLC), in which forty-nine states, the District of Columbia, and the U.S. Territories and Possessions the Virgin Islands, Puerto Rico, the Northern Mariana Islands, Guam, and American Samoa, bringing claims as *parens patriae*, have settled their claims against Hachette, HarperCollins, and Simon & Schuster ("Settlement Action"); and *In re: Electronic Books Antitrust Litigation*, 11 MD 2296 (DLC), in which class action plaintiffs bring claims for damages ("Class Action").

proposed findings of fact and conclusions of law, and pretrial memoranda were submitted on April 26 and, following rulings on redactions, were filed on May 14.

At the time the trial was scheduled, the parties agreed that a bench trial would resolve claims for liability and injunctive relief. With the parties' consent, the trial was conducted in accordance with the Court's customary practices for non-jury proceedings, which includes taking direct testimony from witnesses under a party's control through affidavits submitted with the pretrial order. The parties also served with the Joint Pretrial Order copies of all exhibits and deposition testimony that they intended to offer as evidence in chief at trial.[2]

At trial, the Plaintiffs called twelve fact witnesses and two expert economists. The Plaintiffs' fact witnesses included three Apple employees: Eddy Cue ("Cue"), Senior Vice President of Internet Software and Services at Apple; Keith Moerer ("Moerer"), a Director of iTunes at Apple; and Kevin Saul ("Saul"), Associate General Counsel at Apple, and the lead business

[2] The Court's procedures for non-jury proceedings were discussed in detail at conferences held on June 22 and October 26, 2012, and May 8, 2013. As the parties were informed, the Court prepared a draft opinion in advance of the bench trial based on the witness affidavits and other documents submitted with the pretrial order and the arguments of counsel in their trial memoranda. At trial, the affiants swore to the truth of the contents of their affidavits and were tendered for cross and redirect examination, and the other trial evidence was formally received. The parties understood that the Court's final findings of fact and conclusions of law would incorporate all of this evidence. Consistent with these procedures, and with the expectation that the Court had already prepared a draft opinion, the parties jointly asked the Court for its preliminary views on the merits at the final pretrial conference held on May 23, 2013.

lawyer supporting Apple's Internet and Software Services division. The Plaintiffs also called senior executives from each of the five Publisher Defendants: David Shanks ("Shanks"), CEO of Penguin; Carolyn Reidy ("Reidy"), President and CEO of Simon & Schuster; Brian Murray ("Murray"), CEO of HarperCollins; John Sargent ("Sargent"), CEO of Macmillan; and David Young ("Young"), Chairman and CEO of Hachette from 2006 through March 2013, who currently serves as Chairman of the Board of Directors of Hachette. The Plaintiffs called four additional fact witnesses: Russell Grandinetti ("Grandinetti"), Vice President—Kindle at non-party Amazon.com ("Amazon"); David Naggar ("Naggar"), Vice President of Kindle Content at Amazon; Laura Porco ("Porco"), Amazon's Director of Kindle Books from 2006 to 2011; and Thomas Turvey ("Turvey"), Director of Strategic Partnerships at non-party Google Inc. ("Google"). The Plaintiffs' expert witnesses were Dr. Richard Gilbert ("Gilbert"), Emeritus Professor of Economics and Professor of the Graduate School at the University of California, Berkeley, and a Senior Consultant (Affiliate) at Compass Lexecon, an economic consulting firm; and Dr. Orley Ashenfelter ("Ashenfelter"), the Joseph Douglas Green 1895 Professor of Economics at Princeton University.

Affidavits submitted by the Plaintiffs constituted the direct testimony of four of their fact witnesses—Grandinetti, Naggar, Porco, and Turvey—and both of their expert witnesses. Apple had intended to call seven of Plaintiffs' witnesses in its own case—Cue, Moerer, Murray, Reidy, Sargent, Saul, and Young. Thus, these witnesses' affidavits were also received during the Plaintiffs' case in chief. The Plaintiffs subpoenaed Shanks to testify at trial.[3]

The Plaintiffs also offered excerpts from the depositions of John Makinson ("Makinson"), Chairman and CEO of the Penguin Group, the parent company of Penguin; Arnaud Nourry ("Nourry"), Chairman and CEO of Hachette Livre, the parent company of Hachette; and Maja Thomas ("Thomas"), Senior Vice-President at Hachette. Apple offered counter-designations as to Nourry and Thomas. Each of these witnesses appeared at trial and was cross-examined.

During the presentation of its defense, Apple presented affidavits constituting the direct testimony of three fact witnesses and three expert economists. Apple's fact witnesses were Robert McDonald ("McDonald"), the manager of Apple's U.S. iBookstore; Theresa Horner ("Horner"), Vice President of Digital Content for Barnesandnoble.com, a subsidiary of non-party Barnes & Noble, Inc. ("Barnes & Noble"); and Madeline McIntosh ("McIntosh"), Chief Operating Officer of non-party Random House, Inc. ("Random House"). Apple's expert witnesses were Dr. Benjamin Klein ("Klein"), Professor Emeritus of Economics at the University of California, Los Angeles, Senior Consultant at Compass Lexecon, and President of EAC Associates, Inc.; Dr. Michelle Burtis ("Burtis"), Ph.D., Senior Advisor at Cornerstone Research, Inc., an economic and financial consulting firm; and Dr. Kevin Murphy ("Murphy"), George J. Stigler Distinguished Service Professor of Economics at the University of Chicago, and Faculty

[3] Penguin settled these actions on the eve of trial and therefore the affidavit constituting the direct testimony of Shanks, which had been submitted with the Joint Pretrial Order, was not offered at trial.

Research Associate at the National Bureau of Economic Research. Each of these witnesses, except McIntosh, appeared at trial and was cross-examined. The Plaintiffs did not seek to cross-examine McIntosh.

As noted, the bench trial was held from June 3 to June 20, 2013, and this Opinion presents the Court's findings of fact and conclusions of law. The findings of fact appear principally in the following Background section, but also appear in the remaining sections of the Opinion.

SUMMARY OF FINDINGS

The Plaintiffs have shown that the Publisher Defendants conspired with each other to eliminate retail price competition in order to raise e-book prices, and that Apple played a central role in facilitating and executing that conspiracy. Without Apple's orchestration of this conspiracy, it would not have succeeded as it did in the Spring of 2010.

There is, at the end of the day, very little dispute about many of the most material facts in this case. Before Apple even met with the first Publisher Defendant in mid-December 2009, it knew that the "Big Six" of United States publishing—the Publisher Defendants and Random House (collectively, the "Publishers")—wanted to raise e-book prices, in particular above the $9.99 prevailing price charged by Amazon for many e-book versions of *New York Times* bestselling books ("NYT Bestsellers") and other newly released hardcover books ("New Releases"). Apple also knew that Publisher Defendants were already acting collectively to place pressure on Amazon to abandon its pricing strategy.

At their very first meetings in mid-December 2009, the Publishers conveyed to Apple their abhorrence of Amazon's pricing, and Apple assured the Publishers it was willing to work with them to raise those prices, suggesting prices such as $12.99 and $14.99. Over the course of their negotiations in December 2009 and January 2010, Apple and the Publisher Defendants educated one another about their other priorities. Apple strongly hoped to announce its new iBookstore when it launched the iPad on January 27, 2010, but would only do so if it had agreements in place with a core group of Publishers by that date, could assure itself it would make a profit in the iBookstore, and could offer e-book titles simultaneously with their hardcover releases. For their part, if the Publisher Defendants were going to take control of e-book pricing and move the price point above $9.99, they needed to act collectively; any other course would leave an individual Publisher vulnerable to retaliation from Amazon.

Apple and the Publisher Defendants shared one overarching interest—that there be no price competition at the retail level. Apple did not want to compete with Amazon (or any other e-book retailer) on price; and the Publisher Defendants wanted to end Amazon's $9.99 pricing and increase significantly the prevailing price point for e-books. With a full appreciation of each other's interests, Apple and the Publisher Defendants agreed to work together to eliminate retail price competition in the e-book market and raise the price of e-books above $9.99.

Apple seized the moment and brilliantly played its hand. Taking advantage of the Publisher Defendants' fear of and frustration over Amazon's pricing, as well as the tight window of opportunity created by the impending launch of the iPad on January 27 (the "Launch"), Apple garnered the signatures it needed to introduce the iBookstore at the Launch. It provided the Publisher Defendants with the vision, the format, the timetable, and the coordination that they needed to raise e-book prices. Apple decided to offer the Publisher Defendants the opportunity to move from a wholesale model—where a publisher receives its designated wholesale price for each e-book and the retailer sets the retail price—to an agency model, where a publisher sets the retail price and the retailer sells the e-book as its agent.

The agency agreements that Apple and the Publisher Defendants executed on the eve of the Launch divided New Release e-books among price tiers. The top of each tier, or cap, was essentially the new price for New Release e-books. The caps included $12.99 and $14.99 for many books then being sold at $9.99 by Amazon.

The agreements also included a price parity provision, or Most-Favored-Nation clause ("MFN"), which not only protected Apple by guaranteeing it could match the lowest retail price listed on any competitor's e-bookstore, but also imposed a severe financial penalty upon the Publisher Defendants if they did not force Amazon and other retailers similarly to change their business models and cede control over e-book pricing to the Publishers. As Apple made clear to the Publishers, "There is no one outside of us that can do this for you. If we miss this opportunity, it will likely never come again."

Through the vehicle of the Apple agency agreements, the prices in the nascent e-book industry shifted upward, in some cases 50% or more for an individual title. Virtually overnight, Apple got an attractive, additional feature for its iPad and a guaranteed new revenue stream, and the Publisher Defendants removed Amazon's ability to price their e-books at $9.99. A detailed explanation of how Apple facilitated this conspiracy and changed the face of the e-book industry follows.

BACKGROUND

Defendant Apple engages in a number of businesses, but as relevant here it sells the iPad tablet device and distributes e-books through its iBookstore. E-books are books that are sold to consumers in electronic form, and that can and must be read on a dedicated electronic device such as the iPad, the Barnes & Noble Nook, or Amazon's Kindle. The Publisher Defendants publish both e-books and print books. The five Publisher Defendants and Random House represent the six largest publishers of "trade" books in the United States.[4] These six firms are often referred to within the publishing industry as the "Big Six."[5] The Publisher Defendants sold over 48% of all e-books in the United States in the first quarter of 2010.

A. Development of the E-book Market

Amazon's Kindle was the first e-reader to gain widespread commercial acceptance. When the Kindle was launched in 2007, Amazon quickly became the mar-

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[4] Trade books consist of general interest fiction and non-fiction books. They are to be distinguished from "non-trade" books such as academic textbooks, reference materials, and other texts.

[5] Titles from the Bix Six publishers accounted for over 90% of all U.S. NYT Bestseller book sales in 2010. Random House is the largest of the Big Six, followed, in descending order of size, by Penguin, Simon & Schuster, HarperCollins, Hachette, and Macmillan. When it comes to e-books, the largest of the Big Six in early 2010 was Penguin, followed in descending order by Random House, HarperCollins, Hachette, S&S, and Macmillan.

ket leader in the sale of e-books and e-book readers.[6] Through 2009, Amazon dominated the e-book retail market, selling nearly 90% of all e-books.[7]

Amazon utilized a discount pricing strategy through which it charged $9.99 for certain New Release and bestselling e-books. Amazon was staunchly committed to its $9.99 price point and believed it would have long-term benefits for its consumers. In order to compete with Amazon, other e-book retailers also adopted a $9.99 or lower retail price for many e-book titles.

Prior to April 2010, the Publishers distributed print and digital books through a wholesale pricing model, in which a content provider sets a list price (also known as a suggested retail price) and then sells books and e-books to a retailer—such as Amazon—for a wholesale price, which is often a percentage of the list price. The retailer then offers the book and e-book to consumers at whatever price it chooses. Prior to 2009, many publishers set a wholesale price for e-books at a 20% discount from the equivalent physical book wholesale price to reflect the many cost savings associated with the distribution and sale of e-books. For instance, there is no cost for the printing, storage, packaging, shipping, or return of e-books. With a digital book discount, Amazon's $9.99 price point roughly matched the wholesale price of many of its e-books.

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[6] The Nook was released two years later, in November of 2009, offering some competition to Amazon. The iPad was released in April 2010.

[7] At present, the largest U.S. retailers of trade e-books include Apple, and non-parties Amazon, Barnes & Noble, Google, Kobo Inc., and Sony Corporation.

B. Publishers' Discontent with the $9.99 Price Point

The Publishers were unhappy with Amazon's $9.99 price point and feared that it would have a number of pernicious effects on their profits, both in the short run and long-term. In the short-term, the Publishers believed the low price point was eating into sales of their more profitable hardcover books, which were often priced at thirty dollars or more, and threatening the viability of the brick-and-mortar stores in which hardcover books were displayed and sold. Over the long-term, they feared that consumers would grow accustomed to e-books priced at $9.99 and that the $9.99 price point would erode prices for all books, thereby threatening the business model for the publishing industry. They believed that this low price failed to reflect the true value of many books and also failed to distinguish among books in terms of the effort entailed to create and produce them and in terms of their quality, however one might measure quality.

The Publishers also feared Amazon's growing power in the book distribution business. They were concerned that, should Amazon continue to dominate the sale of e-books to consumers, it would start to demand even lower wholesale prices for e-books and might begin to compete directly with publishers by negotiating directly with authors and literary agents for rights—a process referred to as disintermediation.[8]

As a result, the Publisher Defendants determined that they needed to force Amazon to abandon its dis-

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[8] In fact, as described below, Amazon announced a new initiative in January 2010 that would assist authors in self-publishing through Amazon on the Kindle Digital Platform.

count pricing model. As Hachette's Young bluntly put it, they had to "defea[t] [Amazon's] $9.99 pricing policy," and prevent the "wretched $9.99 price point becoming a de facto standard."

C. January 2009-December 2009: Publisher Defendants Pursue Strategies to Combat Amazon Pricing

Beginning in at least early 2009, the Publisher Defendants began testing different ways to address what Macmillan termed "book devaluation to $9.99," and to confront what S&S's Reidy described as the "basic problem: how to get Amazon to change its pricing" and move off its $9.99 price point. They frequently coordinated their efforts to increase the pressure on Amazon and decrease the likelihood that Amazon would retaliate—an outcome each Publisher Defendant feared if it acted alone.

One of the strategies that they employed was the elimination of the existing discount on wholesale prices of e-books. This meant that the wholesale price for e-books would equal the wholesale price for physical books, and as a result, the wholesale price that Amazon paid for an e-book would be set at several dollars above Amazon's $9.99 price point. This tactic, however, failed to convince Amazon to change its pricing policies and it continued to sell many NYT Bestsellers as loss leaders at $9.99.[9]

The Publishers were not shy about expressing their displeasure to Amazon about its $9.99 pricing. In February 2009, Penguin told Amazon that "their 9.99

[9] Among other strategies that two or more of the Publishers discussed with each other were retail price maintenance, mandatory minimum advertised pricing, and a joint venture to sell e-books.

model" was "not a good sustainable one." HarperCollins similarly warned Amazon that it was "seriously considering changes to our discount structure and our digital list prices for all retailers." In March 2009, Macmillan's Sargent met with Amazon to express his own concern with the $9.99 price point, and indicated that "all the pubs" were talking about it. In June 2009, S&S's Reidy bluntly told Amazon that the $9.99 price point was "a mistake" and that she would "continue to be vocal because she thinks it's terrible for the business." In early December 2009, Hachette's Nourry met with Amazon's Naggar, and told him that Amazon's $9.99 pricing posed a "big problem" for the industry. According to Nourry, if Amazon raised e-book prices by even one or two dollars it would "solve the problem."

The Publisher Defendants did not believe, however, that any one of them acting alone could convince Amazon to change its pricing policy. They also feared that if they did not act as a group, Amazon would use its ever-growing power in the book distribution business to retaliate against them. As a result, the Publisher Defendants conferred about their need to act collectively if they were to have any impact on Amazon's pricing. As a Penguin executive reported to the Penguin Group Board of Directors under the heading "competition and collaboration," it "will not be possible for any individual publisher to mount an effective response" to Amazon "because of both the resources necessary and the risk of retribution, so the industry needs to develop a common strategy."

Thus, as early as December 2008, Stefan von Holtzbrinck of Macmillan and Hachette's Nourry agreed "to exchange information and cooperate very tightly on all issues around e-books and the Kindle." Nourry explained that "at the heart of our strategy" are discussions among "top publishers" in the United States "to create an alternative platform to Amazon for ebooks." He observed, however, that the goal of these ventures is "less to compete with Amazon than to force it to accept a price level higher than 9.99." During the Summer of 2009, Nourry came to New York and met with the CEOs of Hachette's competitors on June 29 and 30. Nourry reported after his first day of meetings that "the movement is positive" with respect to Macmillan, S&S, HarperCollins, and Penguin. While he expressed his continued fear that Amazon's pricing would lead to "selling content at 7$ … [l]ike it works in the music business," he was reassured to know that "none of our competitors" wanted this to happen either.

On a fairly regular basis, roughly once a quarter, the CEOs of the Publishers held dinners in the private dining rooms of New York restaurants, without counsel or assistants present, in order to discuss the common challenges they faced, including most prominently Amazon's pricing policies. Before one such dinner, Hachette's Young promised Nourry that he would raise with his competitors their options to confront the "potentially dominant role played by … Amazon" in e-books, "in order to control their strategy and pricing." As Young put it, "I hate [Amazon's] bullying behavior and will be happy to support a strategy that restricts their plans for world domination."

As the Publisher Defendants' CEOs testified, the Publishers did not compete with each other on price; while they were serious competitors, their preferred fields of competition were over authors and agents. Thus, they felt no hesitation in freely discussing Amazon's prices with each other and their joint strategies for raising those prices.

In the Fall of 2009, Reidy explained to her superior at Simon & Schuster's parent company CBS Corporation, Leslie Moonves ("Moonves"), that S&S was considering several different options to "get Amazon to change its pricing." As Reidy explained,

> we've always known that unless other publishers follow us, there's no chance of success in getting Amazon to change its pricing practices. … And of course you were right that without a critical mass behind us Amazon won't 'negotiate,' so we need to be more confident of how our fellow publishers will react if we make a move."

Reidy assured Moonves, however, that she was "fairly sure that at least two of them would quickly follow us" and would "keep thinking of how to attack the problem (as we perceive it) of current eBook pricing; as you realize, we think it's too important to ignore." Reidy acknowledged to Moonves that "we need to 'gather more troops' and ammunition first!"

In addition to raising the wholesale price of e-books, another strategy that Publisher Defendants adopted in 2009 to combat Amazon's $9.99 pricing was the delayed release or "withholding" of the e-book versions of New Releases, a practice that was also called "windowing."[10] By the end of 2009, four of the Publisher Defendants—Macmillan, Simon & Schuster,

[10] Publishers had traditionally delayed the release of paperback versions of hardcover books. This practice is known as windowing. While the delayed release of some e-book titles, particularly those of popular New Releases, is more technically known as withholding, many in the publishing industry also called it windowing, and that term will also be used in this Opinion to refer to the delayed release of e-books as a strategy employed by the Publisher Defendants to pressure Amazon to lift its e-book prices.

Hachette, and HarperCollins—had announced or implemented a policy of windowing some of their most popular e-book titles on Amazon. By making the more expensive hardcover version available to the public before the lower priced e-book, the Publisher Defendants hoped to protect the sales of New Release hardcover books and to pressure Amazon to raise its e-book prices. Sargent explained his support for withholding e-books from Amazon in the following terms, "Right now it is all about tactics while we try to get hardcovers over the artificially low 9.99 price point," and "we need to do something to budge Amazon from their current strategy." Hachette's Young similarly believed that "windowing … was the only way we could deal with Amazon selling off the family jewels."

In order for the tactic of windowing to succeed, the Publishers knew they needed to act together. That several Publishers synchronized the adoption and announcement of their windowing strategies was thus no mere coincidence. For example, Hachette's Young told Nourry in late Fall 2009, "[c]ompletely confidentially, Carolyn [Reidy] has told me that they [S&S] are delaying the new Stephen King, with his full support, but will not be announcing this until after Labor Day." Understanding the impropriety of this exchange of confidential information with a competitor, Young advised Nourry that "it would be prudent for you to double delete this from your email files when you return to your office." When HarperCollins soon followed with its own windowing announcement, delaying the digital release of Sarah Palin's *Going Rogue*, Hachette's Nourry congratulated Murray on his decision: "Well done for the Palin book," Nourry wrote, "and welcome to the Club!"

The Publisher Defendants' synchronized windowing strategy was publicly reported and tied to their discontent with Amazon's pricing. A *Wall Street Journal* article of December 9, entitled "Two Major Publishers to Hold Back E-Books," reported that S&S was windowing in order to "tak[e] a dramatic stand against the cut-rate $9.99 pricing of e-book best sellers," and that Hachette would follow suit in an effort to "preserve our industry" from authors' work being "sold off at bargain-basement prices." The article's author noted that "publishers have come to fear that the bargain prices will lead consumers to conclude that books are worth only $10, or less, upsetting the pricing model that has survived for decades." The article reported that S&S was intentionally focusing its windowing efforts on its most popular titles; as an S&S executive explained, she was concerned that e-book sales were "cannibalizing new best-selling hardcovers, which are the mainstay of the publishing business."

A *New York Times* article of the same day entitled "Publishers Delay E-book Releases," described an even broader effort among the Publisher Defendants to delay the digital release of certain popular titles. It reported that "[p]ublishers have been debating the timing of e-books in part as a way to protest the low prices—typically $9.99—that online retailers like Amazon and Sony are offering on ebook versions of new releases and best sellers." It stated that at least four Publishers—S&S, Hachette, HarperCollins, and Macmillan—already had begun or announced an intention to window e-books in the coming year. The article described the economics of windowing and tied the strategy to the protection of Publishers' physical book business, stating that

> Although publishers currently receive the same wholesale price for an e-book that they receive for a print book (meaning the retailer takes a loss on the sale of the most popular e-

> books), publishing houses worry that eventually, Amazon and other e-book retailers will pressure publishers to take a smaller cut on e-books. In addition, since 95 percent of the business still comes from print booksellers, the publishers want to prevent those retailers from reducing orders.

The next day, the *Wall Street Journal* similarly announced that others had joined the windowing movement, reporting that "HarperCollins Joins Ranks of Those Delaying E-Books," as "the debate over the timing and pricing of e-books heats up." The article stated that, beginning in early 2010, HarperCollins will delay the release of "five to ten hardcover titles each month." It quoted Murray saying, "We have to believe that delaying the e-book edition helped hardcover sales." The article also reported that Penguin was "watching the current situation with interest."

The three Publisher Defendants who had announced their adoption of a windowing policy hoped that Macmillan, Penguin, and Random House would join their campaign. As Nourry expressed on December 6, in order "[t]o succeed our colleagues must … follow us." Five days later, S&S's Reidy advised Macmillan that it would "love" for Macmillan "to join" Hachette, HarperCollins, and S&S in windowing, and "fel[t] if one more publisher comes aboard, everyone else will follow suit." On December 15, Macmillan announced that, starting in January, it would delay release of most of its e-books for 90 days.[11] It was reported in the *Wall Street Journal* on December 16.

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[11] As it turned out, Macmillan never implemented this policy.

This left only two of the Big Six not yet committed to windowing. Penguin's Makinson reported in December that Hachette had started to "put a lot of pressure" on Penguin "to join the windowing movement," but Penguin refused to do so. Penguin's McCall was well aware that "[i]f other publishers don't follow suit" with windowing, Amazon's $9.99 "predatory pricing will continue, and we'll lose." When Penguin and Random House chose not to join their competitors and delay the release of e-books, Hachette's Young found their refusal "deeply divisive and disappointing."

Even though by the Winter of 2009, four of the Publisher Defendants had delayed the release of some e-books or announced an intention to so, they knew that windowing was not a long-term solution to Amazon's $9.99 pricing model. Among other things, windowing carried serious risks. As Sargent recognized, windowing was "really bad" because it encouraged piracy. Reidy noted that windowing "did not seem the wisest course" since "it doesn't seem smart to penalize the eBook reader: we in fact want to encourage eBook purchases, so long as we can maintain our margins and income." She feared that windowing could "alienate an entire portion (and a growing one) of our audience." As Sargent admitted to an author on December 14, while windowing could be used as a short-term tactic, "[w]indowing is entirely stupid," and "actually makes no damn sense at all really." As a Penguin study showed, when a Publisher delayed the release of e-books, its sales never recovered. The lost customers neither bought the print book at a higher price nor returned to purchase those e-books when they finally became available.

Sargent, for one, hoped that over time Publishers would be able to move to a system of simultaneous release of e-books with their physical counterparts, but at a higher price point of between $12.95 and $14.95. In order to do so, the Publishers would need to find a way to gain long-term control over pricing, including on Amazon. "The questions is," Sargent wondered, "how to get there?" Other Publisher Defendants envisioned even higher price points for e-books, but pondered the same fundamental dilemma. It was in this context that Apple arrived on the scene and provided the Publisher Defendants with the means to achieve their shared goal.

D. Apple's Development of iBooks

Apple is one of America's most admired, dynamic, and successful technology companies. Its innovative devices are immensely popular not only in this country but around the world. But, as of 2009, Apple had no e-bookstore. Consumers could read e-books on Apple's devices through third party software, such as apps, but Apple did not yet have its own e-reading software or e-bookstore with a collection of books available for purchase.

Apple did not have an e-bookstore in 2009 because it did not yet have a device that its founder Steve Jobs ("Jobs") believed would be a great e-reader. He demanded no less before he would invest his company's energies in e-books. That was about to change.

In 2009, Apple was close to unveiling the iPad. With this revolutionary tablet, Apple was able to contemplate the arrival of its first great device for reading e-books. Therefore, under the direction of Apple's Cue, Moerer and others began studying the e-book industry. As of 2009, Cue had worked at Apple for twenty years and had played a major role in creating Apple's content stores, beginning with Apple's Online Store in 1998, the iTunes Store in 2003, and the App Store in 2008. Since

2004, Cue had been responsible for running all of Apple's digital content stores and had led Apple's negotiations in its deals with major content providers.

By June, Cue's team had assembled data that showed that the book market in North America was larger than the music market. The book industry was estimated to be roughly $35 to $42 billion in size, with trade books comprising $12.5 billion of that figure. While trade e-books accounted for just $100 million or so of those numbers, that market was growing at an exponential rate. Apple's McDonald predicted that the e-book market could reach nearly $1 billion in 2010.

Apple, of course, knew that Amazon was the dominant e-retailer ("e-tailer") of books. While part of Amazon's success could be attributed to its Kindle, Apple understood that another reason for Amazon's success in the e-book market was its low prices. As of that time, Apple had little experience with competing on price when selling content; indeed, it considered itself a price "leader" in selling music, apps, and other content.

It was also clear to Cue that "all the content owners hate Amazon."[12] As early as February 2009, Cue recognized that "[t]he book publishers would do almost anything for us to get into the ebook business." Apple had also discovered analyst reports in June 2009 that indicated that a price of $12.99 could be a more profitable price point for e-books than Amazon's $9.99.

By November 2009, Apple had compiled a "Business Outlook" for audio book and e-book opportunities. It concluded that selling e-books as individual apps was

[12] Cue attributed the Publishers' hatred of Amazon to Amazon "leveraging [its] force in physical [books] to force [the Publishers] into bad deals" in e-books.

"flawed." It was at that relatively late date that Jobs authorized Cue to pursue the development of a dedicated Apple e-bookstore (the "iBookstore") for the iPad. Apple planned to demonstrate the iPad to the public at the Launch on January 27, 2010, and planned to ship the devices to stores in early April 2010.

Apple believed that the iPad would be a transformational e-reader. In contrast to the black-and-white e-reader devices on the market at the time, the iPad would have the capacity to display not only e-book text but also e-book illustrations and photographs in color on a backlit screen. The iPad would also have audio and video capabilities and a touch screen, which Apple believed would be seen by readers as a particularly attractive feature.

Even though the iPad Launch would happen with or without an iBookstore, Apple did hope to announce its new iBookstore at the Launch. This would ensure maximum consumer exposure and provide a dramatic component of the Launch. But, this left Cue with less than two months for Apple to acquire enough content to create a viable Apple e-bookstore, and that period included the Christmas and New Year holidays.[13] As a result, Apple streamlined its efforts and concentrated on executing agreements with the Big Six Publishers for trade e-books. It would broaden its campaign to add more publishers and to include other kinds of e-books, including textbooks and every other kind of e-book, after the Launch.

[13] The record does not reveal when Apple began to develop the software for the iBookstore, but it is clear that Apple was intensely engaged in that development throughout this two month window.

Cue also had his own reasons for working hard to make the iBookstore a reality in time for the Launch. He was, of course, an able and experienced negotiator. He took pride in all he had achieved for Apple and wanted to succeed in adding an e-bookstore to its other content domains. Cue believed that with the introduction of the iPad the iBookstore held the potential to be another rousing success for his company. But, beyond professional pride, Cue had more personal reasons for making the iBookstore a reality in record-breaking time. Cue knew that Jobs was seriously ill and that this would be one of his last opportunities to bring to life one of Jobs's visions and to demonstrate his devotion to the man who had given him the opportunity to help transform American culture.

E. December 15 to 16, 2009: Apple's First New York Meetings with Publishers

Beginning on December 8, 2009, Cue's team contacted the Publishers to set up meetings the following week to discuss an "extremely confidential" subject. Apple made it clear in these calls that it would be trying to meet with each of the Big Six CEOs on its whirlwind trip to New York City.

Apple's requests for meetings in New York was an exciting turn of events for the Publishers and prompted a flurry of telephone calls among them. They speculated about how they might turn Apple's entry into the e-book business to their advantage in their battle with Amazon. They were well aware of the press reports that Apple would be announcing the arrival of another revolutionary device. Reidy, Murray, and Young exchanged at least five telephone calls on December 10 and 11 alone. These calls among the Publisher Defendants' CEOs would continue and intensify at critical moments during the course of the Publishers' ensuing negotiations with Apple.[14] *See* Appendix A.

Even before it met with any of the Publishers on December 15, Apple already knew several things that are important to the events that would unfold in the coming weeks. As previously described, Apple understood that the Publishers wanted to pressure Amazon to raise the $9.99 price point for e-books, that the Publishers were searching for ways to do that, and that they were willing to coordinate their efforts to achieve that goal. By December 15, the *Wall Street Journal* and *New York Times* articles of December 9 and 10 had described the windowing commitment made by three of the Big Six. Cue viewed the e-book market at the time to be dysfunctional and ripe for Apple's arrival.

For its part, Apple had decided that it would not open the iBookstore if it could not make money on the store and compete effectively with Amazon.[15] Apple knew that it needed access to a large number of titles. It was unwilling to allow e-books to be windowed at any Apple store. Apple also preferred to sell e-books at prices below their physical counterparts, although that object largely fell by the wayside in the coming weeks.

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[14] The telephone calls among the Publisher Defendants during the period of their negotiations with Apple represented a departure from the ordinary pattern of calls among them. By contrast, there was only one telephone call made between these CEOs during the week prior to Apple's first contact with the Publishers on December 8.

[15] Some months earlier, Apple had considered proposing to Amazon that they simply divide the e-market for books and music, with iTunes acting as "an ebook reseller exclusive to Amazon and Amazon becom[ing] an audio/video iTunes reseller exclusive to Apple."

Prior to meeting with the Publishers, Apple assumed that it would purchase e-books from them under the wholesale model and resell them, in line with the arrangement Apple used to obtain movies and TV shows for resale through its iTunes store.

As a master negotiator, Cue came well prepared for his meetings. He knew how to convey Apple's conditions for entry and at the same time give the Publishers an incentive for entering, almost overnight, into a partnership with Apple. He decided to entice the Publishers by conveying an unambiguous message that Apple was willing to sell e-books at prices up to $14.99, that is, at a price point $5 above Amazon's price for many New Releases and NYT Bestsellers.

Cue, Moerer, and their in-house attorney Saul met separately with Hachette, Penguin, and Random House on December 15, and with HarperCollins, Macmillan, and S&S on December 16. If there was one Publisher that Apple most desired to have in its iBookstore, it was Random House, the largest Publisher. As events unfolded, however, that would be the only Publisher who declined to join the iBookstore before the Launch.

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.

The parties exchanged thoughts about a workable business model in these meetings. Apple learned that current wholesale prices for e-books typically fell in the range of $13 to $15, and some were even sold at prices as high as $17.50. Cue told Publishers that they would need to lower their wholesale prices for Apple if Apple were to enter the business. In order for Apple to compete with Amazon it needed to be able to price e-books as cheaply as Amazon did, and it was not willing to pursue a strategy of loss leaders. As Reidy recorded, Apple expressed that it "cannot tolerate a market where the product is sold significantly more cheaply elsewhere."

Well aware of the Publishers' experimentation with windowing, Apple also told Publishers that it opposed windowing; it believed that withholding e-books alienated customers and led to piracy. Random House and Macmillan agreed, telling Apple that they believed windowing was "a terrible, self-destructive idea," even though Macmillan admitted that it might be considering "holdbacks" on some NYT Bestsellers.

Hachette and later HarperCollins surprised Apple with their suggestion that, instead of a wholesale model, Apple adopt an agency model for the distribution of e-books. Hachette told Apple that it had already discussed switching to an agency model with Barnes & Noble and had concluded that it was an attractive business model for selling e-books.[16] During these meet-

[16] Hachette's Thomas had spoken to a HarperCollins executive on December 10, in advance of their meetings with Apple, regarding exploring agency as an alternative business model.

ings, Cue rejected the idea. Within days, however, he would reconsider their suggestion.

Mainly, however, the Publishers told Apple how unhappy they were with Amazon's $9.99 price point. Every Publisher with whom Apple met lamented Amazon's pricing New Releases and NYT Bestsellers at $9.99. Several of them made clear that they were actively searching for a way to gain more control over pricing and were implementing tactics they did not enjoy, like windowing, in an attempt to effect the change that was of utmost importance to them.

For example, Penguin in its meeting with Apple shared its view that a $9.99 e-book was not a "sustainable model." The next day, S&S frankly admitted "hating" Amazon pricing, and HarperCollins revealed that it was interested in the agency model in order "to fix Amazon pricing." HarperCollins advocated that e-book prices be set in the range of $18 to $20, which Cue viewed as utterly unrealistic. Listening to the Publishers, Cue understood that they were afraid that Amazon's pricing strategy threatened their overall business.

Apple, in turn, assured the Publishers that it was not interested in entering the e-book market by pursuing a low-price strategy. Apple opined that $9.99 was not yet "engrained" in the consumer mind, and suggested in each meeting pricing e-books at between $11.99 and $14.99. The Publishers were thrilled. Macmillan agreed immediately with Apple's suggested $14.99 retail price for New Releases.

As Cue promptly reported to Jobs on December 15, after he had completed the first three of his six meetings, "[c]learly, the biggest issue is new release pricing and they want a proposal from us." Cue was confident that he would be able to build the iBookstore in time for the Launch. As he told Jobs, "[n]othing scared me or made me feel like we can't get these deals done right away." In his view, the Publishers had been "ecstatic" about what Apple's arrival could mean for "their industry."

On the heels of their initial meetings with Apple, the Publisher Defendants enthusiastically shared the good news that Apple was willing to enter the e-book market with a significantly higher price point for newly-released e-books. On December 17, Reidy reported the "[t]errific news!" to Moonves that Apple was entering the e-book market and "was not interested in a low price point for digital books." Reidy understood that "they [Apple] don't want Amazon's $9.95 to continue." Hachette's Nourry similarly told Cue after their initial meeting that he was glad it appeared "our business interests are very much aligned." HarperCollins later reflected that Apple was the Publishers' "best partner" because it "do[es]n't like deep discounting."

Several of the Publishers hashed over their meetings with Apple with one another. After Young had met with Apple but before S&S had its meeting, Young could not resist calling Reidy to share the wonderful news that the "Top Man" at Apple opposed $9.99 pricing. He hesitated to say more because S&S would be meeting with Apple the following day, and he did not want to "spoil [the] fun." Young and Reidy promised to "check in" with each other after S&S had its meeting with Apple, and did so in several calls over the course of the next two days.[17] At a breakfast meeting, Pen-

[17] On December 15, Hachette's Young spoke to S&S's Reidy by telephone prior to his meeting with Cue. On December 16, Reidy called Young just minutes after her meeting with Cue had ended. The next day, the two exchanged three calls.

guin's Makinson discussed the Apple meetings with Hachette's Nourry. On December 17, Rupert Murdoch, Chairman and CEO of HarperCollins' parent company News Corp, relayed to Random House that Apple would soon be launching an e-reader and would be "selling books at 15 dollars." Charlie Redmayne, a HarperCollins' digital officer, bluntly suggested to Murray immediately after their meeting with Apple on December 16 that they coordinate a response to Apple with the other Publishers. As Redmayne wrote, in light of their "[g]reat meeting … I wou[]ld talk to the other CEO's early and look to present in early Jan."

F. Apple Switches Gears and Presents An Agency Model with 30% Commission

Having received an enthusiastic reception from the Publishers, the Apple team returned to Apple's headquarters in Cupertino, California and quickly absorbed what it had heard. One idea that it considered proposing to the Publishers, but rejected, was an across-the-board 25% discount for e-books off the wholesale price for physical books. With many NYT Bestsellers having a $12 wholesale price for the hardcover book, this would allow a $9 digital wholesale price, which Apple's Moerer thought should be "acceptable" to the Publishers for all of their e-books with the possible exception of a few blockbusters.

Cue quickly decided, however, to go a different route. Unless the Publishers agreed to lower wholesale prices for e-books, Apple would run the risk of losing money if it tried or was forced to match Amazon's pricing to remain competitive. The wholesale model also allowed the Publishers to try to control digital book prices by windowing e-books. As Apple had expressed to the Publishers, it strongly believed that withholding content would interfere with the growth of the digital market and was inconsistent with its business goals and practices. Apple thus embraced the model that Hachette and HarperCollins had proposed—the agency model. Apple was already familiar with this model since it used the agency model to sell apps through its App Store.

Apple realized that the recent turmoil in the digital book business strengthened its hand in proposing this new business model to the Publishers. Apple did not have to open an e-bookstore when it launched the iPad; it could add the iBookstore later. On the other hand, the Publishers were searching for an alternative to Amazon's pricing policies and excited about Apple's entry into the e-book industry and the prospect that that entry would give them leverage in their negotiations with Amazon. Apple appreciated that, in the words of Macmillan's Sargent, the Publishers viewed Apple as "offer[ing] the single best opportunity [they] would ever have to correct the imbalance in our e-book market."

Apple settled on an agency model with a 30% commission, the same commission it was using in its App Store. Agency would give the Publishers the control over e-book pricing that they desired, and ensured that Apple would make a profit from every e-book sale in its iBookstore without having to compete on price. Apple realized, however, that in handing over pricing decisions to the Publishers, it needed to restrain their desire to raise e-book prices sky high. It decided to require retail prices to be restrained by pricing tiers with caps. While Apple was willing to raise e-book prices by as much as 50% over Amazon's $9.99, it did not want to be embarrassed by what it considered unrealistically high prices.

The agency model presented one significant problem. Apple wanted its iBookstore to be a rousing success. For that to happen, Apple needed not only content but also customers. Apple realized that if it moved to an agency model with the Publishers, Apple would be at a competitive disadvantage so long as Amazon remained on the wholesale model and could price New Releases and NYT Bestsellers at $9.99, or even lower to compete with Apple. Since it was inevitable that the Publishers would raise e-book prices when given the opportunity—indeed, Apple expected the Publishers to raise the prices to the tier caps—e-books priced at $9.99 by Amazon would doom the iBookstore. Why would a consumer buy an e-book in the iBookstore for $14.99 when it could download it from Amazon for $9.99?

To ensure that the iBookstore would be competitive at higher prices, Apple concluded that it needed to eliminate all retail price competition. Thus, the final component of its agency model required the Publishers to move all of their e-tailers to agency. Apple expected that this proposal would appeal to the Publishers. After all, it would allow them to "fix" their "problem" with Amazon's pricing.

Apple's first meetings with the Publishers in New York had occurred on a Tuesday and Wednesday. Just three days later, on Saturday, Cue was ready to test drive his agency model and hear preliminary reactions from the Publishers. On December 19, Cue emailed three of the six Publishers' CEOs to set up thirty minute meetings for the following Monday or Tuesday to "update you [on] all my findings and thoughts." Cue already knew from the meetings earlier in the week that Hachette and HarperCollins were enamored of the agency model and did not contact them again at this stage. He had pegged Penguin's CEO as a "follower," and chose to hold off on contacting him. After all, Penguin and Random House were the only Publishers that had not publicly announced any plans to withhold e-books from Amazon. Cue decided instead to test his proposal with S&S, Macmillan, and Random House.

Cue chose these three Publishers carefully. He considered Reidy a real "leader" among her fellow CEOs. He was not wrong. As described below, she was instrumental in convincing both Penguin and Macmillan to sign up with Apple when they were wavering. She was in frequent contact with Young, Shanks and Sargent at every critical juncture in the weeks before the Launch.

Cue reached out to Macmillan's Sargent for a different reason. He had been impressed with Sargent's personal history, in particular his family's storied connection with the publishing industry.[18] Cue believed that a partnership with Macmillan would add caché. But, most importantly, Cue wanted the largest Publisher, Random House, to come on board.

Cue succeeded in speaking with key executives from each of these three Publishers early the following week. He explained that he had met with all of the Big Six the preceding week, and had come to the conclusion that the way forward would involve four components. First, the e-book "industry" needed to move to the agency model, which would allow the Publishers to set the prices and introduce what Cue euphemistically termed "some level of reasonable pricing." Second, Apple would need a 30% margin on e-books sold through Apple. Third, he proposed setting prices for

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[18] Sargent's father, John Turner Sargent, Sr., was the President and CEO of the Doubleday & Company publishing house from 1963 to 1978, and led the company's expansion into an industry giant.

New Release e-books at $12.99, that is, $3 over Amazon's $9.99 price. Finally, to remove all retail price competition, the Publishers would have to adopt the agency model for all of their e-tailers.

Reidy described her conversation with Cue in a detailed email to colleagues at S&S that day. According to Reidy, Cue "didn't think anything [other than the agency model] would keep the market from its current pricing 'craziness.'" Reidy did not hesitate over the suggestion that the industry as a whole be moved to an agency model; Reidy had replied to Cue, "if we make these our terms, then they are our terms." Overall, Reidy was intrigued, but worried that the 30% commission for Apple would be too "steep."

Markus Dohle ("Dohle"), Chairman and CEO of Random House at the time, similarly described his conversation with Cue to colleagues at Random House. Dohle reported that Cue "thinks that book prices are becoming too low—he is worried about the consumer perception. Therefore he suggests an 'agency model.'" Eliminating price competition with Amazon was essential to Cue since "[h]e assumes that if we find a new TOS [terms of sale, wholesale] model which would provide A[pple] with an acceptable margin, Amazon would lower the prices again following … their loss leader[] strategy." As Dohle reported, when he expressed concern about Amazon's willingness to accept an agency model, Cue suggested that "windowing could be used to establish a distributor [agent] model" if Amazon balked.

Shortly after his conversation with Cue, Sargent wrote to Cue to suggest a pricing strategy that would allow Publishers to price some e-books at $19.95, but that "put the majority of new releases at the 14.95 or 12.95 price points." Introducing the concept of a dual model, an idea that would continue to have appeal for Sargent in the following weeks, Sargent also suggested that Apple offer two alternative terms of sale—a "30% agency model with no windowing," and "[a] [d]iscount model that includes windowing"—allowing each Publisher to "decid[e] which model to buy under." Sargent later reflected to another Macmillan executive that he believed this dual approach "[w]ould force Amazon's hand."

On December 21, Cue advised Jobs that his talks with the Publishers had gone "well and everyone understood our position and thought it was reasonable." Cue observed that the Publishers recognized "the plus" of moving to an agency model, namely it "solves Amazon issue."[2719] On the "negative" side, they were troubled by

[19] Cue asserted at trial that "solves Amazon issue" referred to pricing e-books in the iBookstore above $9.99, and was not a reference to raising prices across the industry or eliminating Amazon's ability to set prices. Indeed, Cue protested at trial that, throughout its negotiations with the Publisher Defendants, Apple was concerned only with the pricing that would prevail in the iBookstore and sought only to "fix" Amazon's pricing or "solve the Amazon issue" in its own e-bookstore. In this and several other aspects of Cue's testimony, regrettably, he was not credible. The documentary record and the commercial context of the negotiations leave room for no other conclusion. Apple's pitch to the Publishers was—from beginning to end—a vision for a new industry-wide price schedule. Any other course would have left the Publishers vulnerable to Amazon's pricing strategies and would have forced Apple to compete on price. Accordingly, Cue's repeated assertion at trial that his sole "focus" was on thinking about the agency deals and their effects "from an Apple point of view," cannot be taken at face value. As a savvy negotiator he knew how to place himself in the Publishers' shoes, understand their interests, and appeal to their concerns, as he eventually admitted toward the end of his testimony. Cue recognized that the Publishers were consumed first and foremost by a desire to eliminate Amazon's $9.99 price for e-books across the market. His colleagues, includ-

a commission for Apple that was as high as 30%. That gave the Publishers a "little less" than they would like. As of that point, Cue believed that the Publishers were willing to pursue a strategy of moving all of their e-tailers to the agency model, and in fact several Publishers had told him so. The Publishers believed, however, that a $12.99 price for an e-book would be too low if the physical book sold for more than $35. Cue reported that he had urged them to focus "on the other 99% and we can figure out how to solve the exceptions" later.

Buoyed by the reactions of the three Publishers to Apple's proposal that the entire e-book industry be converted to an agency model—with higher prices for e-books, a 30% commission for Apple and no retail price competition—Cue's team turned their energies toward fleshing out a structure for this arrangement. They entered the Christmas break with every hope that an iBookstore could be announced at the Launch.

G. Apple's Term Sheet: All E-tailers to Agency and Pricing Caps

Shortly after the Christmas holidays, Cue wrote to each of the Publishers to present Apple's term sheet. On January 4 and 5, the first Monday and Tuesday in the new year, Cue wrote six essentially identical emails.[20] Only the introduction varied. For the three Publishers with whom he had talked in late December,

ing Saul, acknowledged that they understood at the time that Apple could not solve the Publisher's problem with $9.99 if the Publishers left Amazon on wholesale. Thus, Cue and his team found a way to solve the "Amazon problem" for the Publishers; not just "as to Apple," but industry-wide.

[20] Cue sent emails to Macmillan, S&S, Random House, and Hachette on January 4. Cue's emails to Penguin and HarperCollins were sent on January 5.

Cue began his emails with, "As we discussed." For the other three, he began with the following comment: "After talking to all the other publishers and seeing the overall book environment, here is what I think is the best approach for ebooks."[21]

In these emails, Cue recapped the key components of Apple's proposed agency model. It included the elimination of retail price competition and raising many e-book prices by at least $3. Cue wrote, "Just like the App Store, we are proposing a principal-agency model with you, where you would be the principal and iTunes would sell your product as your agent for your account. In exchange for acting as your agent iTunes would get a 30% commission for each transaction." For "hardback books" that retail for less than $35, the Publisher would set a price for an e-book at any price up to $12.99; for trade or mass-market paperback books, the price would be capped at $9.99; and for any book that retailed above $35, the e-book price would be capped at $14.99 and increments of $5 above that. Cue added that a "realistic" price for an e-book would be less than 50% of the retail price for the hardcover book. He emphasized that "to sell e-books at realistic prices … all resellers of new titles need to be in agency model." In closing, Cue reiterated that Apple "think[s] these agency terms accomplish[] all the goals we both have."

It was as apparent to the Publishers as it was to Apple that Apple's proposal would only allow the Publishers to raise the consumer prices for e-book versions of their key titles above Amazon's $9.99 price point to the proposed price caps if they moved Amazon and

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[21] For reasons unknown, Cue sent two emails to Macmillan, one with each greeting.

their other e-tailers to agency. Reidy immediately advised her S&S colleagues that she was "in total agreement" that the "[a]gency model should hold for all retailers; these would become our terms." Reidy's notes on her copy of Cue's e-mail captured the benefits she saw accruing from Apple's proposal. The ability to raise e-book prices and protect the physical book business was front and center. Her notes read: "Higher price slows Ebks/casual purchaser/keeps retailers/stops authors leaving."

In the conversations that followed the dissemination of the term sheet, Publishers told Apple that the proposed price caps were too low. Apple reiterated that it would not tolerate windowing, it did not want to lose money, and it did not want any price competition. It advocated for an industry-wide adoption of the agency model as "the only way" to "move the whole market off 9.99."

H. Creation of the MFN Clause

One week after it distributed the term sheet, Apple distributed a draft contract. During the intervening week, however, Cue's thinking about how to achieve an industry-wide shift to the agency model changed. His in-house counsel had been working on an alternative way to reach that goal that was even more effective in protecting Apple's interests. Saul proposed using an MFN clause for retail prices. The MFN guaranteed that the e-books in Apple's e-bookstore would be sold for the lowest retail price available in the marketplace.

Apple had used an MFN in one of its music agreements, but the music had been purchased under a wholesale model. Apple's use of an MFN for a retail price was a unique feature of its e-book agency agreements.

By combining the MFN with the pricing tiers, the pricing discretion Apple gave to the Publishers with one hand, it took away with the other. While Publishers could theoretically raise e-book prices in the iBookstore above the $9.99 price point to the top of the Apple pricing tiers, unless the Publishers moved all of their e-tailers to an agency model and raised e-book prices in all of those e-bookstores, Apple would be selling its e-books at its competitors' lower prices. Using Saul's characterization, the "elegant" solution presented by the MFN accomplished all of Apple's objectives. It eliminated any risk that Apple would ever have to compete on price when selling e-books, while as a practical matter forcing the Publishers to adopt the agency model across the board. As Cue admitted to colleagues in Britain in the Spring, "any decent MFN forces the model."[22]

Cue had an opportunity to explain the concept of the MFN to Moerer on January 10. Moerer had been speaking with Random House, which was increasingly skeptical of Apple's proposals, and he wanted Cue's advice on how to respond to several of its questions. One question was, "Are we willing to accept an agency model if other retailers continue a standard wholesale model for new releases without holdbacks?" Cue responded, "We are (I don't think we can legally force this).[2823] What we care about is price so the contract will say we

[22] Cue's words are captured in a colleague's memorandum. At trial, Cue denied that he had actually spoken in those terms.

[23] Apple takes the position that Cue's explanation that it couldn't "legally force" the Publishers to place all of their e-tailers on an agency contract is not a reference to the lawfulness of such a requirement, but is instead a reference to Apple's skepticism that it could legally enforce the clause against any Publisher who reneged on its commitment. It is unnecessary to resolve this ambiguity.

get it at 30% less whatever the lowest retail price out in the market is (whether agency or wholesale)."

With the adoption of the MFN, Apple dropped from the agency contract it was drafting the explicit requirement that had appeared in its term sheet that all e-tailers be placed on an agency model. But, Apple did not change its thinking. It believed that the Publishers should still move their e-tailers to agency, and in the weeks that followed, it made sure that happened. Cue was able to report to Jobs on January 13, three days after his e-mail exchange with Moerer, that at least two of the Publishers had agreed to "go [to the] agency model for new releases with everyone else." Thus, despite the fact that it would tell Random House during its increasingly difficult negotiations that it could accept a hybrid model where Random House moves to agency with Apple but stays on wholesale with some retailers, there is no evidence that Apple ever communicated to any of the Publisher Defendants that they were free to leave their other retailers of e-books on a wholesale model or that Apple ever rescinded its demand that each of them move to an agency arrangement with all resellers.[24]

As described above, Apple, quite simply, did not want to compete with Amazon on price. Apple was confident that the iPad would be a revolutionary and wild-

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[24] A great deal of time was spent at trial trying to understand a series of five emails drafted by Jobs on January 14. Cue wanted Jobs's approval for higher price caps, and Jobs's emails show that he was quite concerned about the profitability of the iBookstore. Jobs's final email in the chain indicates that the Publishers need to "move Amazon to the agent model too for new releases for the first year. If they don't, I'm not sure we can be competitive." The e-mails were addressed to Cue and he denies ever receiving any of them, including the last in the series.

ly popular device. It was happy to compete with Amazon on that playing field, where it believed its strength resided. It would match its device—the iPad—against the Kindle. As HarperCollins executive Robert Zaffiris observed on January 20, "Apple is cutting a blanket agency deal to level the playing field and ultimately compete in two areas they feel good about—technology and iTunes."

I. January 11: Apple Distributes Draft Agency Agreements

On Monday, January 11, Apple sent its proposed eBook Agency Distribution Agreement ("Draft Agreement") to each of the Publishers. With the iPad launch just sixteen days away, Cue told Jobs that his "goal" was to "get at least 2 of them to sign this week."

The Draft Agreement contained all of the essential elements of the contracts that the Publisher Defendants would accept two weeks later, including a "day and date" commitment to prohibit windowing on the Apple iBookstore,[25] price tiers, the 30% commission, and the MFN. Although the Publisher Defendants were able to negotiate around the edges, none of the material terms of the contract changed. Apple insisted that its agency contract be uniform. It assured the Publisher Defendants that they would all be getting the same terms, as would every other publisher who decided to sell e-books through the iBookstore.

In the end, each of the Publisher Defendants simply had to decide whether they wanted to take this opportunity to raise the price of e-books or not. The risks of acting and of failing to act were similarly large. As

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[25] The day and date commitment required Publishers to give Apple e-books on the same date they released physical books.

explained below, if a Publisher accepted Apple's terms it was bound to lose some of the revenue it would otherwise make from selling e-books, and could be assured that it would incur the wrath of Amazon. If the Publisher declined to join Apple it would lose this particular opportunity, backed by Apple, to confront Amazon as one of an organized group of Publishers united in an effort to eradicate the $9.99 price point.

In the two intervening weeks before the Launch, Apple and the Publishers engaged in intensive negotiations. Apple's Cue, Moerer, and Saul stayed in New York for the nine days immediately preceding the Launch to conclude the negotiations. Up until the very end, it was not clear precisely how many of the five Publisher Defendants would agree to execute the agency contract with Apple.

By all accounts, the negotiations were tough, particularly because Apple made few concessions. The Apple team reminded the Publishers though that this was a rare opportunity for them to achieve control over pricing. As Cue put it bluntly to Hachette, the agency model proposed by Apple was "the best chance for publishers to challenge the 9.99 price point." Some of the discussions regarding three contract terms—the MFN, the 30% commission, and the pricing tiers—are described here.

1. *MFN Negotiations*

The MFN clause required publishers to match in Apple's iBookstore any lower retail price of a New Release offered by any other retailer. The proposed MFN read: "If, for any particular New Release in hardcover format, the then-current Customer Price at any time is or becomes higher than a customer price offered by any other reseller ("Other Customer Price"), then Publisher shall designate a new, lower Customer Price to meet such lower Other Customer Price." Customer Price was defined as "the price displayed to the [customer] on the [Apple] Online Store, as designated by [the] Publisher for each eBook by selecting from the prices set forth" in an exhibit to the contract.

As already described, the MFN effectively forced the Publisher Defendants to change their entire e-book distribution business to an agency model if they wanted to take control of retail pricing. Any other course would be a race to the bottom in e-book prices and would give the Publisher Defendants a fixed share of a far too small revenue stream.

Under the then-existing wholesale model for selling e-books, the Publisher Defendants received a designated wholesale price for each e-book. This wholesale model was more profitable for a Publisher's e-book business than the agency model proposed by Apple. Under a wholesale arrangement a Publisher received roughly 50% of the hardcover list price from the retailer, whereas under Apple's agency arrangement a Publisher received only 70% of the retail price. For example, as shown on this table, a Publisher might receive $13 on a wholesale basis for an e-book sold by Amazon for $9.99, but (because of the MFN) only $7 from Apple so long as Amazon was still selling that e-book for $9.99. Even if Apple and Amazon were on the same agency arrangement with a Publisher, and that Publisher were able to move the retail price of the e-book to the top of the Apple price tier and sell it for $12.99, the Publisher would still receive less revenue under the agency model: $9.10 instead of the $13.00 in revenue under the wholesale model.

Publisher Per Unit Earnings
for New Release and NYT Bestseller Titles
Wholesale vs. Agency Model

	Amazon on Wholesale prior to Apple's entry	Apple on Agency with MFN; Amazon on Wholesale	Apple and Amazon on Agency with MFN and Apple price tiers
Hardcover list price	$26.00	$26.00	$26.00
E-book wholesale price (assuming 50%)	$13.00	$13.00	--
Amazon retail price	$9.99	$9.99	$12.99
Apple iBookstore retail price	--	$9.99	$12.99
Publisher revenue received from Amazon	$13.00	**$13.00**	**$9.10**
Publisher revenue received from Apple	--	**$7.00**	**$9.10**

Because the revenue each Publisher Defendant would receive per e-book sold through the Apple store was substantially less than what it was currently receiving under its wholesale arrangements, there was no financial incentive for a Publisher to sign an agency agreement with Apple unless those agreements suited its long-term interests. And as Apple well understood, that long-term interest was compelling. The Publisher Defendants wanted to shift their industry to higher e-book prices to protect the prices of their physical books and the brick and mortar stores that sold those physical books. While no one Publisher could effect an industry-wide shift in prices or change the public's perception of a book's value, if they moved together they could.

To change the price of e-books across the industry, however, the Publishers would have to raise Amazon's prices. This is where the MFN became such a critical term in Apple's contracts with the Publisher Defendants. It literally stiffened the spines of the Publisher Defendants to ensure that they would demand new terms from Amazon. Thus, the MFN protected Apple from retail price competition as it punished a Publisher if it failed to impose agency terms on other e-tailers.

Many of the documents received into evidence at trial as well as trial testimony reflect this understanding. After signing the Agreement, HarperCollins acknowledged that "[t]he Apple agency model deal means that we will have to shift to an agency model with Amazon" to "strengthen our control over pricing."

Penguin's CFO acknowledged on February 15, 2010, "[g]iven the clauses about price matching in the Apple contract, this could mean that we have to suspend or delay certain sales of e-books to Amazon until the contract is renegotiated" to move Amazon to the agency model. Recognizing the compulsive nature of the MFN, Shanks testified that in evaluating the Apple deal he came to understand that "the only way we could do [agency]" was if Penguin moved to agency with other e-book retailers as well.

Reidy testified that the MFN meant, as a practical business matter, that S&S would be moving all its other e-book retailers to agency "unless we wanted to make even less money." As Reidy had written to Moonves, remaining on a wholesale model with Amazon "would just enshrine the $9.99 price point at a later date and would require us to lower our own pricing to those who accept the agency model to that price point." Reidy knew that once S&S signed its Agreement with Apple, "we need to change our ebook selling terms with our other eRetailers before" the iBookstore opened, or risk "a situation whereby we must price our adult new release eBooks sold through Apple at $9.99, undercutting one of the reasons for making the deal."

Young also understood that the MFN required Hachette to move all of its e-book retailers to an agency relationship, and "ensure," in his words, "a competitive, level playing field for e-book sellers."[26] Fully recognizing the benefits and risks from the Apple offer, Nourry told Young that he was "not against [the] MFN as long as it is legal" because "[w]e need to find higher pricing points."[2927]

Cue explained that the Publisher Defendants generally did not fight him on the MFN.[3028] He was even told that it was an unnecessary feature of the contract since the Publishers were going to move to an agency relationship with all e-book retailers anyway.

The final agency agreements with the Publisher Defendants (the "Agreements") included an MFN in paragraph 5(b). Although there were variations among the five paragraphs, the core principle of the MFN remained intact. The MFN assured that Apple would face no retail price competition and that the Publisher Defendants had no choice but to demand that Amazon, and every other e-book retailer, adopt the agency model. As Saul insisted in an e-mail to an independent publisher who was frustrated that the MFN removed the publisher's control over pricing, "There are possible unilateral ways you can comply with our [MFN] provision, such as get others on an agency model, or with-

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[26] The word "competitive" in this and many other contexts at the trial means the opposite of competition. It means the eradication of retail price competition.

[27] Macmillan also identified that the antitrust risk of signing the agency agreement with the MFN could be "huge."

[28] Although Cue attempted to deny this fact at trial, at his deposition Cue admitted that the Publisher Defendants generally "accepted" the MFN, and although the term was negotiated, Cue never felt it was discussed "in [the] completely material way of saying, no, we're not doing that." Instead, the conversations were focused mainly on "trying to create loopholes or exceptions to it."

hold content. Others have agreed to this and we cannot make any changes."

2. *30 Percent Commission Negotiations*

The 30% commission on which Apple insisted in its agency agreements meant that any increase in retail prices, even up to the caps of the pricing tiers, would not compensate for the revenue loss the Publisher Defendants would experience from the sale of e-books under the agency model. Some of the Publisher Defendants predicted that the loss would be roughly 17% of their e-book gross revenue and amount to millions of dollars.

HarperCollins' Murray immediately recognized that "[t]he combination of Apple's proposed pricing tiers and the 30% commission meant that HarperCollins would make less money per book than it was then making on a wholesale model." To address this problem, HarperCollins suggested that Apple take a commission of just 20%.

Apple refused to budge. This was the same commission it charged in the App Store. It would give Apple only a single digit positive margin and, in Apple's view, was necessary to generate the revenue Apple needed to build a great iBookstore. The 30% commission was ultimately adopted across all of Apple's final Agreements.

3. *Price Tier Negotiations*

The Publisher Defendants fought hardest over the price caps. They and Apple knew that these negotiations were really about setting the new industry prices for e-books.

These negotiations were intense even though the Draft Agreement included more generous price tiers than the term sheet had proposed.[3129] The Draft Agreement capped e-book prices at $12.99 for New Release titles with hardcover list prices of $30 or under, and set a $14.99 price tier cap for New Release titles with hardcover list prices above $30, with incremental price tier increases for every $5 increase in the hardcover list price above $30. For books other than New Releases, the price cap was set at $9.99.

To dramatize the immediate increase in the price of e-books that the Publishers could achieve under the Apple agency agreement, and to assure each Publisher Defendant that it was being treated no differently than its competitors, Moerer sent a table of proposed book prices to them in identical e-mails on the same day Apple sent out the Draft Agreements. The table showed fiction NYT Bestsellers from every member of the Big Six. It listed the book's title, author, and publisher. It showed each title's hardcover list price, followed by its retail prices when sold as an Amazon hardcover book; Amazon e-book; Barnes & Noble e-book; and finally, as a proposed iTunes e-book.[3230] The proposed prices under the iTunes column were always either $12.99 or $14.99, and were always several dollars higher than the then-existing e-book price at Amazon and Barnes &

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[29] The January 4 term sheet had set a price cap at $14.99 for any book with a hardcover list price above $35, and $12.99 for any hardcover book listed below $35. The Draft Agreement, by contrast, set the demarcation between $12.99 and $14.99 at $30, allowing for higher e-book prices in relation to a title's hardcover list price.

[30] Sensitive to the fact that the table looked like an Apple retail price list, Moerer clarified in a follow-up email to Shanks that the prices in the table's final column designating the "iTunes eBook Retail Price" are the "top price tier we've proposed" and that "[i]n the agency model, Penguin would set retail prices at its sole discretion, at this price or any lower price, with Apple acting as your agent."

Noble. In some cases, the iTunes e-book price was even higher than the Amazon hardcover price.[3331] While the final column would only display Apple's e-book prices for titles published by the particular Publisher receiving that version of the table, the layout made it easy for the Publishers to see that they were all being treated identically. The first page of one of these tables is set out below.

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[31] The Amazon price for e-books, by contrast, was always lower than its retail price for a title's corresponding physical book.

Subject: our meeting tomorrow
Date: Mon, 11 Jan 2010 14:34:29 -0800
From: Keith Moerer <kmoerer@apple.com>
To: <david.shanks@us.penguingroup.com>
Cc: Eddy Cue <cue@apple.com>
Message-ID: <75004564-BE31-48CE-A0EC-EC9ECC98D588@apple.com>

David--

I look forward to meeting with you and Genevieve tomorrow morning.

Kevin Saul has sent a draft agreement in separate email. Eddy has also asked me to send you our pricing analysis of Jan. 1 NYT bestsellers, which will help explain the price tiers we've proposed for hardcover new releases.

Best, Keith

NYT Bestsellers-Hardcover Fiction	Title	Author	Publisher	Hardcover List Price	Amazon Hardcover Retail Price	Amazon eBook Retail Price	B&N eBook Retail Price	iTunes eBook Retail Price
	The Lost Symbol	Dan Brown	Random House	$29.95	$12.00	$9.60	$9.60	
	I, Alex Cross	James Patterson	Hachette	$27.99	$16.79	$9.99	$9.99	
	Under the Dome	Stephen King	Simon & Schuster	$35.00	$21.00	$9.99	$9.99	
	The Help	Kathryn Stockett	Penguin	$24.95	$9.50	$8.55	$8.55	$12.99
	Pirate Latitudes	Michael Crichton	HarperCollins	$27.99	$14.00	$9.99	$9.99	
	Ford County	John Grisham	Random House	$24.00	$11.00	NA	NA	
	U is for Undertow	Sue Grafton	Penguin	$27.95	$14.96	$9.99	$9.99	$12.99
	The Last Song	Nicholas Sparks	Hachette	$24.99	$12.96	$8.80	$8.80	
	The Christmas Sweater	Glenn Beck	Simon & Schuster	$19.99	$11.97	$9.99	$9.99	
	Breathless	Dean Koontz	Random House	$28.00	$14.00	$9.99	$9.99	
	The Lacuna	Barbara Kingsolver	HarperCollins	$26.99	$13.00	$9.99	$9.99	
	True Blue	David Baldacci	Hachette	$27.99	$13.97	$9.99	$9.99	
	Wolf Hall	Hilary Mantel	Macmillan	$27.00	$11.00	$8.80	$8.80	
	The Gathering Storm	Robert Jordan	Macmillan	$29.99	$17.54	NA	NA	
	Half Broke Horses	Jeannette Walls	Simon & Schuster	$26.00	$14.46	$9.99	$9.99	
	Pursuit of Honor	Vince Flynn	Simon & Schuster	$27.99	$12.47	$8.00	$8.00	
	The Scarpetta Factor	Patricia Cornwell	Penguin	$27.95	$14.97	$9.99	$9.99	$12.99
	The Girl Who Played with Fire	Stieg Larsson	Random House	$25.95	$13.00	$7.99	$7.99	
	The Wrecker	Clive Cussler	Penguin	$27.95	$15.97	$9.99	$9.99	$12.99
	South of Broad	Pat Conroy	Random House	$29.95	$16.97	$9.99	$9.99	
	Last Night in Twisted River	John Irving	Random House	$28.00	$15.97	$9.99	$9.99	
	Too Much Happiness	Alice Munro	Random House	$25.95	$15.17	$9.99	$9.99	
	Nanny Returns	Emma McLaughlin	Simon & Schuster	$25.00	$14.39	$9.99	$9.99	
	Too Much Money	Dominick Dunne	Random House	$26.00	$15.21	$9.99	$9.99	
	Her Fearful Symmetry	Audrey Niffenegger	Simon & Schuster	$26.99	$13.49	$5.79	$5.79	
	Heat Wave	Richard Castle	HarperCollins	$19.99	$11.69	$9.99	$9.99	
	Divine Misdemeanors	Laurell K. Ballantine	Random House	$26.00	$14.97	$9.99	$9.99	

Penguin, HarperCollins, Hachette, and S&S quickly told Apple that they were willing to do an agency model for New Releases, and that they would "go with" the agency model with "everyone else," but that they needed higher price caps. The debate over the caps essentially ended on Saturday, January 16. This was five days after the Draft Agreements had been distributed. Despite their efforts, the Publisher Defendants achieved only modest adjustments to the price caps.

On January 16, Cue sent nearly identical e-mails to each of the Publisher Defendants with a revised pricing proposal. Under this new regime, Cue decreased the hardcover list price triggers for the $12.99 and $14.99 e-book caps a second time, but carved out NYT Bestsellers for special treatment. When a NYT Best-seller was listed for $30 or less, the iTunes price would be capped at $12.99; when it was listed above $30 and up to $35, the iTunes price would be no greater than $14.99.[3432] For all other New Releases, the caps in the Draft Agreement would be applied to physical books with slightly lower list prices. For example, the $12.99 cap now applied to titles with list prices between $25.01 and $27.50 instead of those at $30 or less; the $14.99 cap applied to books with list prices between $27.51 and $30 instead of over $30. Cue also added two additional price caps at $16.99 and $19.99 for books listed between $30.01-$35 and $35.01-$40, respectively.

In his e-mails to the Publisher Defendants, Cue outlined the advantages he perceived they would gain from Apple's entry into the market, defended the pricing tiers of $12.99 and $14.99 for NYT Bestsellers, explaining that "it is critical that we appear at least reasonable" in relation "to the heavy discounting that is happening for NYT bestsellers." Cue added that, "This gives you significantly more tiers and higher prices." Except for small exceptions which were immaterial to Apple, this pricing proposal was the one finally adopted in the Agreements.

Cue had described these tiers to Jobs as prices that would "push [the Publisher Defendants] to the very

[32] Cue's January 16 offer kept the price caps for NYT Bestsellers at the caps listed for all New Releases in the Draft Agreement.

edge," but still create a "credible offering in the market." Cue warned Jobs that "[t]his will be hard to get because they [the Publishers] will be losing an additional $1.40, but we should try."

Further confirming that Apple well understood that the negotiations over the price "caps" were actually negotiations over ultimate e-book prices, Cue's calculation of the $1.40 loss arose from his proposal that the prices of the NYT Bestsellers be capped at prices lower than other New Releases at similar hardcover list prices, and lower than the Publisher Defendants had been expecting. If a New Release with a list price of $30 or less was a NYT Bestseller, the cap moved from $14.99 to $12.99, meaning that the Publisher would receive 70% of $12.99 instead of 70% of $14.99, or $1.40 less.

Cue was right to expect pushback from the Publishers over the carve-out for NYT Bestsellers. Hachette's Thomas identified the ceilings of $14.99 and $12.99 for NYT Bestsellers as a drawback when writing to her colleagues on January 19. Thomas warned that these prices would represent a "significant" loss to Hachette's profit margin.

The Publisher Defendants recognized that Apple's pricing regime would be a game-changer for the e-book industry. Because these caps would become the new standard industry-wide prices, they continued to push for higher ceilings. As Hachette's Nourry testified, the whole concept of price "caps," when coupled with the Publishers' move to an agency model of distribution, was that "people all have the same prices." Nourry was thus particularly "reluctant to fixing best seller prices at 12$90" with Apple "because it may be our last chance to bring it back up to say 14$99."

HarperCollins similarly understood that the "upshot" of the Apple agreement "is that Apple would control price and that price would be standard across the industry." Indeed, it believed that the benefit of moving to an agency model with Apple's price cap structure was the creation of "uniform prices" for e-books and an "increase" in price "from 9.99 to 12.99 or 14.99 for most books."[3533]

Ultimately, the Publisher Defendants all capitulated to Cue's revised pricing regime. Even though Penguin's McCall still wanted to see all NYT Bestsellers capped at $14.99, he recognized on January 19 that Apple's proposal of $12.99 was "probably the middle ground where compromise is going to have to happen." The reference to "middle ground" was a reference to the spread between Amazon's $9.99 price for the e-book version of NYT Bestsellers and the Barnes & Noble price for the physical book version. He observed as well that "[i]f we migrate all accounts to agency selling, the price spread shouldn't matter, since we'll have a level playing field."

Macmillan was also unhappy with the price caps proposed by Apple. It opposed the concept of price caps in general, but, as Sargent recognized, Apple wanted the price caps "as protection against excessively high prices that could either alienate [its] customers or subject [it] to ridicule." S&S accepted the price caps proposed on January 16 on the condition that Apple would agree to "review pricing" after one year on the new model. Cue readily agreed.

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[33] Through a process known as translation, the prices for digital books are automatically set according to a predetermined relationship to the prices of their physical counterparts.

The January 16 pricing tiers were incorporated into Apple's final Agreements and were identical for each Publisher Defendant. Through Apple's adoption of price caps in its Agreements, it took on the role of setting the prices for the Publisher Defendants' e-books and eventually for much of the e-book industry. As described below, the Publisher Defendants largely moved the prices of their e-books to the caps, raising them consistently higher than they had been albeit below the prices that they would have preferred.

As of January 16, the Launch was just eleven days away and Cue did not have a single Agreement executed. At that point, he had set a deadline of Thursday, January 21, as the final date by which the Publishers had to sign agency agreements with Apple.[3634] As noted above, Cue and his team came to New York for this final push. They arrived on Monday, January 18, and stayed until January 26, the day before the Launch. By January 26, Apple had executed its fifth Agreement.

J. January 18-27: Publishers Initiate Agency Negotiations with Amazon

As already recounted, this entire endeavor was shaped by the Publishers' desire to raise the price of e-books being sold through Amazon. With nearly a 90% market share for e-books in 2009, Amazon was the single most important seller of e-books in America, and also a dominant seller of physical books. Because of this power, the Publishers feared retaliation from Amazon unless they acted in unison. The confrontation with Amazon

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[34] Cue wanted to be sure he had the Agreements in place early enough so that Jobs could finalize his presentation introducing the iBookstore during the Launch.

began the week of January 18, before any of the Publisher Defendants had actually signed an Apple Agreement.

Press reports on January 18 and 19 alerted the publishing world and Amazon to the Publishers' negotiations with Apple. A *Wall Street Journal* article titled "Publisher in Talks with Apple Over Tablet" reported on January 18 that HarperCollins and Apple were in discussions over an agency relationship and that this shift might mean higher prices for e-books. The article explained that "HarperCollins is expected to set the prices of the e-books … with Apple taking a percentage of sales," and noted that "[o]ther publishers have also met with Apple." The article reported that "enhanced" e-book new releases could be priced as high as $14.99 or $19.99.[3735] A detailed article on January 19 in the trade publication *Publishers Lunch* also reported that the Big Six were negotiating terms with Apple that would give them an opportunity to impose an agency model on the entire industry and to raise prices.

On the night of January 18, Amazon received confirmation from a former colleague who was now working at Random House that most of the Publishers were likely to enter agency agreements with Apple. Random House's McIntosh confirmed to Amazon's Porco that several of the Publisher Defendants were negotiating e-book agency distribution agreements with Apple and that Random House "was under pressure from other publishers" to join them. Porco was concerned that Random House would be the only Publisher who decid-

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[35] While Murray chose to describe the price increases as related to e-books "enhanced" with special features, in fact the price increases implemented through the Apple Agreements applied to all e-books.

ed to keep the "current model" that allowed retailers like Amazon make pricing decisions.

Amazon was adamantly opposed to adoption of the agency model and did not want to cede pricing authority to the Publishers.[3836] On January 20, Amazon disclosed how it would respond. It would appeal directly to authors and encourage something the Publishers feared: disintermediation.

That day, Amazon announced that authors and publishers of Kindle e-books could choose a "new 70 percent royalty option" for e-books with a list price "between $2.99 and $9.99." Under this option, the author would receive 70% of the list price, net of delivery costs. Using as an example an e-book being sold for $8.99, the author would make just $3.15 under the standard option, but $6.25 with the "new 70 percent option."

This was not happy news for the Publishers. With an author receiving $6.25 of $8.99, and Amazon keeping the rest, this amounted to a naked play to eliminate the Publishers as a middle-man between authors and Amazon. Shanks observed, "On Apple I am now more con-

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[36] Apple has suggested that Amazon was less opposed to the agency model than the evidence shows. It points to a single brainstorming session between two Amazon employees in early 2009, in which they tried to come up with ideas to mollify the Publishers. The two employees pondered whether the Publishers would agree to accept a flat percentage of the retail price for e-books and quickly dismissed the idea since it would mean a significant loss of revenue for the Publishers. This was not a discussion of the agency model; there was no discussion about Amazon ceding control over the retail price. There is simply no credible evidence that Amazon moved willingly to the agency model in 2010. On January 31, 2010, after the Publisher Defendants executed the Agreements, these two individuals expressed astonishment that Publishers had agreed to a deal that resulted in a significant loss of revenue for them.

vinced that we need a viable alternative to Amazon or this nonsense will continue and get much worse." HarperCollins' parent News Corp also reacted with anger. News Corp's Rupert Murdoch called HarperCollins to complain and in no uncertain terms expressed a desire to take revenge on Amazon.

During this week, Amazon had a long-scheduled set of meetings in New York with the Publishers. In separate conversations on January 20 and over the next few days, the Publisher Defendants all told Amazon that they wanted to change to an agency distribution model with Amazon. HarperCollins had a particularly contentious meeting with Amazon on January 20, when it told Amazon that it "had to" move to agency.[3937] Amazon made clear that it preferred to continue to do business on the wholesale model.

On January 22, alluding to its negotiations with Apple and the deadline associated with the impending Launch, HarperCollins outlined its terms in writing to Amazon. The message referred to the "tremendous change" occurring in the e-book industry "this week and next week." It warned that Amazon had to act quickly since

> [d]eliberations are moving fast. If I could get your support to this kind of agency model in principle, I have less need to support other partners who wish to enter the ebook business. As I mentioned we haven't made any decisions yet about how we will sell ebooks to consumers yet, but decision time is approaching.

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[37] In internal emails that morning, HarperCollins executives explained that a "big win of the Agency model is that by us setting price we can protect the value of our hard covers."

Attempting to leverage its Apple negotiations to get a better deal with Amazon, HarperCollins included a proposed retail price for the majority of titles at either \$12.99 or \$14.99, but a commission of just 5% for Amazon. HarperCollins then leveled its threat to Amazon. If Amazon declined its offer, HarperCollins would delay for six months the release of any e-book sold on a wholesale basis.

On January 20, Amazon also met with Macmillan. At a lunch between Macmillan's Sargent and Amazon's Grandinetti, Sargent announced that Macmillan was planning to offer Amazon the option to choose either an agency and reseller model. But, Sargent was mistaken. Neither Apple nor his fellow Publisher Defendants would allow Amazon the option of remaining on a wholesale model. At a dinner that night, Cue explained to Sargent that Macmillan had no choice but to move Amazon to an agency model if it wanted to sign an agency agreement with Apple. The next morning, on January 21, Sargent wrote to Cue and in a carefully crafted message admitted that he had "misread" Cue in their previous discussions, and warned that "[t]he stumbling block is the single large issue we clearly had a misunderstanding about." That stumbling block was "significant enough for us that we may in fact give you a no later today." Referring to the commitment to move all resellers of e-books to an agency model, Cue responded that afternoon that he "d[id]n't believe we are asking you to do anything, you haven't told us you are doing. We are just trying to get a commitment." He requested that they all "sit down … and talk through it."[4038]

[38] Neither Sargent nor Cue was credible during the trial when they denied that Cue had explained at dinner that Macmillan was required to put Amazon on the agency model. Sargent protested

Cue also enlisted Sargent's competitors to intercede with him: Cue spoke with Reidy, the CEO he considered a leader in the industry, for over twenty minutes after receiving Sargent's email on January 21. Cue also called Murray immediately after hanging up with Reidy, and they talked for ten minutes later that day. At that point, Cue called Sargent and urged him to speak with Murray and Reidy. Sargent spoke to both Murray and Reidy by telephone for eight and fifteen minutes, respectively.

The straight talk from Reidy, Murray, and Cue worked.[4139] 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.

Amazon received a virtually identical message from a third Publisher Defendant on January 20. Hachette told Amazon that day that it was looking at the agency

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that he could not remember the conversation, even though his email on the following day referred to "the single large issue" that might lead Macmillan to abandon its negotiations with Apple. Cue explained in his deposition that the biggest issues during his negotiations with Macmillan were the MFN and price tiers, and that he thought the discussion at dinner had been about pricing tiers; then at trial explained that he now remembered that they had discussed one-off promotions. Cue's contemporaneous notes, however, indicate that the core issue in dispute with Macmillan was, in fact, the MFN and its implications. In an email to Jobs on the evening of January 21, just hours after sending his email to Sargent, Cue reported that "[a]fter a long afternoon with their general counsel, we are in agreement on the terms" with Macmillan, "but the CEO and GC have legal concerns over the price matching."

[39] While Murray was fully supportive of the requirement that all e-tailers be moved to an agency model, as described below, he remained unhappy over the size of Apple's commission and the existence of price caps.

model, and believed that it could offer only one pricing model to retailers, either the agency or reseller model, but not both.

On Friday, January 22, S&S's Reidy advised Amazon that it was likely to move its entire business to the agency model. Amazon asked if it could continue to sell under the wholesale model after a window of ninety days. Reidy said she would look at the idea, but did not actually consider it to be a realistic option since it "would just enshrine the $9.99 price point at a later date." Amazon's Grandinetti expressed appreciation for the call, but said he was not sure "what this would mean in terms of our overall relationship." Reidy explained her expectations about pricing going forward, and underscored that she did not intend to go as low as $9.99.

Thus, by the end of that week, four of the five Publisher Defendants had put Amazon on notice that they were joining forces with Apple and would be altering their relationship with Amazon in order to take control of the retail price of e-books.[4240] It was clear to Amazon that it was facing a united front.

K. January 21-26: Execution of Agreements

Even though Apple had told the Big Six in December that it needed all of them to sign on in order to open its e-bookstore, on January 21 it learned that Random House, the largest Publisher, would not sign an agency agreement. Apple decided to proceed without Random House. It let the Publisher Defendants know about Random House's decision and of its own decision to proceed with an iBookstore so long as four of them agreed to its terms before the Launch. In the days that

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[40] Amazon had reached out to Penguin during that period, but Penguin had not responded.

followed, Apple kept the Publisher Defendants apprised about who was in and how many were on board.

The Publisher Defendants kept each other informed as well. 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. In the critical negotiation period, over the three days between January 19 and 21, Murray, Reidy, Shanks, Young, and Sargent called one another 34 times, with 27 calls exchanged on January 21 alone.[4341]

On Thursday, January 21, Cue briefed Jobs on the status of his negotiations with the Publishers.[4442] Cue was confident that S&S and Penguin would sign. Penguin did not want to be alone, but Cue predicted that if he had secured as few as two other Publishers, Penguin would sign on. Cue reported that Hachette and Macmillan had legal concerns over the "price matching," that is, the MFN. HarperCollins was still trying to get Apple to accept a 10% commission on New Releases and to shorten the definition of a New Release to a title that had been in the market two months.[4543] Cue be-

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[41] While many of these calls were simply efforts to reach the other person, those efforts and the conversations that occurred during some of them reflect the intensity of the communications in this period.

[42] At this stage, it was Cue's judgment that Random House would wait until after the Launch to make a decision whether to convert to the agency model. Cue relayed Random House's email describing its "excitement" about Apple entering the market and "building a bookstore", but expressing several reservations about Apple's terms.

[43] The "new release" period would be set in the final Agreements at seven months.

lieved that the Publishers' hesitation to make a commitment to Apple was due to their fear over how difficult it was going to be to force Amazon to convert to an agency relationship. As Cue explained, "[i]n the end, they want us and see the opportunity we give them but they're scared to commit! It [has] less to do with the terms and more about the dramatic business change for them. … They just have to get some balls."

By Friday evening, January 22, Cue was able to report progress. He informed Jobs that he had commitments from Hachette, S&S, Macmillan, and Penguin that they would sign. At this point, Penguin required assurance that three other Publishers were also signing Agreements. As Cue admits, in these final days the Publishers needed reassurance that they would not be alone in signing an agency agreement with Apple because they feared Amazon's reaction, reassurance that Cue readily provided.

The first Publisher to agree to Apple's terms was S&S. S&S signed its Agreement on Monday, January 25. Reidy advised Moonves that at the Launch Apple would announce that NYT Bestsellers would be priced at $12.99.

Hachette's Young had agreed to sign by January 22, but needed approval from France. Hachette executed its Agreement on January 24. As Nourry explained, Hachette signed the Agreement because the agency model "will put an end to price deflation …. We do not like the 12,90 price point, but it is much better than 9,99." Hachette also committed to Apple that it would move all of its relationships with distributors to an agency relationship.

On January 21, Cue sent substantively identical e-mails to Macmillan and Penguin stating that Apple had completed its first agency agreement and was "very close" on two more. By the next day, January 22, Macmillan had agreed to the deal. As Cue told Sargent, Macmillan was the third Publisher to agree to Apple's terms. Macmillan executed the Agreement on January 25. Macmillan's Sargent testified that he decided to sign the Agreement even though he was "not completely happy with some of Apple's terms," because it was a "much better business strategy than simply continuing the status quo with Amazon."

On January 22, Penguin's Shanks had asked Cue whether Apple had "any more of the [B]ig [S]ix confirmed yet?" Even though three other Publishers had joined with Apple by the morning of January 25, a Monday, Penguin was still hesitant. Shanks wanted assurance that he could price e-book versions of paperbacks, particularly trade paperbacks, above $9.99. Once again, S&S's Reidy played a pivotal role. Cue called Shanks, and the two spoke for twenty minutes that morning. Less than an hour after getting off the telephone with Cue, Shanks called Reidy to discuss Penguin's status in its negotiations with Apple. By that afternoon, Penguin had executed its Agreement. Penguin advised Apple that it would be moving to an agency arrangement with all of its e-tailers.

That same day, Penguin reported to its board that when Apple announces "its long-awaited entry into the e-reader market" on Wednesday, "you may also see in the media that Penguin, along with a few other major trade publishers, has made a partnership with Apple for the sale of US eBooks in the iTunes store." The report explained the agency model it had agreed to adopt with Apple, and stated that "we don't think [the agency model and the discount model we currently use with Amazon] for eBooks can coexist very long, and so we're going to be telling all our re-selling middlemen (Amazon, Barnes & Noble, e.g.) that we're going to deal with them for eBooks on the agency basis in the future, too." At its next "Road Show" Penguin credited Apple with its own decision to begin the "monumental effort" of moving its other e-tailers to agency. It reported that, in light of the "pending release of the iPad," and "[a]s a way to enter the market place, Apple proposed moving the entire industry to an agency model."

HarperCollins was the last of the five Publisher Defendants to agree to execute an Agreement. As late as Friday, January 22, Murray wrote to Cue to thank him for his visit that morning, but to underscore HarperCollins' demands. HarperCollins wanted "flexibility" on price outside the tiers; it wanted to sell through other "agents" at a higher price than the retail prices in the iBookstore; it wanted to limit the commission to 10%; and it wanted a shorter "new release window." Reflecting his understanding that his company would be trying to get all of its distributors to adopt an agency relationship, Murray explained, "We need to have flexibility on the agency window. We believe this window should be 6 months rather than 12 months in the event that one or more large retailers do not move to an agency model."

Cue was concerned that HarperCollins wanted to "drive ebook prices sky high." So, Cue suggested that Jobs call James Murdoch of News Corp, HarperCollins' parent company, and "tell him we have 3 signed so there is no leap of faith here."[4644]

[44] Jobs and Cue had met James Murdoch for the first time on January 14, when representatives from News Corp had visited Apple's Cupertino headquarters to discuss a broad range of mutual business interests.

Jobs called Murdoch on January 22 about HarperCollins' intransigence. While Murdoch wanted to do business with Apple, he remained concerned about the economics of the deal, as he described in some detail in an email he sent to Jobs. Jobs's lengthy response on Saturday, January 23, included the following:

> 1. The current business model of companies like Amazon distributing ebooks below cost or without making a reasonable profit isn't sustainable for long. As ebooks become a larger business, distributors will need to make at least a small profit, and you will want this too so that they invest in the future of the business with infrastructure, marketing, etc.
>
> 2. All the major publishers tell us that Amazon's $9.99 price for new releases is eroding the value perception of their products in customer's minds, and they do not want this practice to continue for new releases.
>
> 3. Apple is proposing to give the cost benefits of a book without raw materials, distribution, remaindering, cost of capital, bad debt, etc., to the customer, not Apple. This is why a new release would be priced at $12.99, say, instead of $16.99 or even higher. Apple doesn't want to make more than the slim profit margin it makes distributing music, movies, etc.
>
> 4. $9 per new release should represent a gross margin neutral business model for the publishers. We are not asking them to make any less money. As for the artists, giving them the same amount of royalty as they make today, leaving the publisher with the same profits, is as easy as sending them all a letter telling

them that you are paying them a higher percentage for ebooks. They won't be sad.

5. Analysts estimate that Amazon has sold slightly more than one million Kindles in 18+ months (Amazon has never said). We will sell more of our new devices than all of the Kindles ever sold during the first few weeks they are on sale. If you stick with just Amazon, B&N, Sony, etc., you will likely be sitting on the sidelines of the mainstream ebook revolution.

6. Customers will demand an end-to-end solution, meaning an online bookstore that carries the books, handles the transactions with their credit cards, and delivers the books seamlessly to their device. So far, there are only two companies who have demonstrated online stores with significant transaction volume—Apple and Amazon. Apple's iTunes Store and App Store have over 120 million customers with credit cards on file and have downloaded over 12 billion products. This is the type of online assets that will be required to scale the ebook business into something that matters to the publishers.

So, yes, getting around $9 per new release[45] is less than the $12.50 or so that Amazon is currently paying. But the current situation is not sustainable and not a strong foundation upon which to build an ebook business. And the amount we will pay should be gross margin neutral. Apple is the only other company cur-

[45] Jobs's reference to $9 in revenue is a reference to the 70% of a $12.99 e-book price that a Publisher would receive under Apple's agency Agreement.

> rently capable of making a serious impact, and we have 4 of the 6 big publishers signed up already. Once we open things up for the second tier of publishers, we will have plenty of books to offer. We'd love to have HC among them.

Murdoch still demurred, particularly with respect to Apple's proposed price points, so Jobs wrote again on the morning of January 24.

> Our proposal does set the upper limit for ebook retail pricing based on the hardcover price of each book. The reason we are doing this is that, with our experience selling a lot of content online, we simply don't think the ebook market can be successful with pricing higher than $12.99 or $14.99. Heck, Amazon is selling these books at $9.99, and who knows, maybe they are right and we will fail even at $12.99. But we're willing to try at the prices we've proposed. We are not willing to try at higher prices because we are pretty sure we'll all fail.
>
> As I see it, HC has the following choices:
>
> 1. Throw in with apple and see if we can all make a go of this to create a real mainstream ebooks market at $12.99 and $14.99.
>
> 2. Keep going with Amazon at $9.99. You will make a bit more money in the short term, but in the medium term Amazon will tell you they will be paying you 70% of $9.99. They have shareholders too.
>
> 3. Hold back your books from Amazon. Without a way for customers to buy your ebooks, they will steal them. This will be the start of piracy and once started there will be no

> stopping it. Trust me, I've seen this happen with my own eyes.
>
> Maybe I'm missing something, but I don't see any other alternatives. Do you?

On January 23, Cue had sent his own message to Murray. "I wanted to let you know that we have 4 publishers completed so it is real shame" to not have an agreement with HarperCollins. The next day, Cue also wrote to an executive at News Corp. He expressed that Apple "think[s] our customers will pay a reasonable price (… 50-100% more than existing e-books)" and candidly laid out Apple's "basic deal points," including that Apple is offering "new release hardback pricing maximums which are way higher than $9.99 -> &12.99 or $14.99 for most."

Murray had a round of telephone calls with other Publisher Defendants prior to signing. In the end, HarperCollins concluded that the deal Apple was offering was the best it could get at that time. It considered the economics of the deal to be "terrible" for it and its authors but "the strategic value" of creating an Apple e-bookstore to be "very high." It principally feared "Amazon[']s reaction," but as the fifth Publisher to adopt an agency agreement with Apple, it hoped the reaction would be "muted." Ultimately, HarperCollins understood this was a "once-in-a-lifetime chance to flip the model." On January 26, the day before the Launch, HarperCollins became the fifth Publisher Defendant to accept the Agreement.

The only Publisher to decline to sign the Agreement was Random House. As noted, it had informed Apple of its decision on January 21. Apple had been as inflexible in its bargaining with Random House as it had been with the Publisher Defendants. Random House declined to adopt the Agreement for several reasons. It believed it "would be better off economically sticking with the wholesale model." It also realized that it was not well equipped at that time to set efficient retail prices, and that it would be necessary to make a "complete switch to agency" if it entered into an agency agreement with Apple, which it was not prepared to do.

Thus, in less than two months, Apple had signed agency contracts with five of the six Publishers, and those Publisher Defendants had agreed with each other and Apple to solve the "Amazon issue" and eliminate retail price competition for e-books. The Publisher Defendants would move as one, first to force Amazon to relinquish control of pricing, and then, when the iBookstore went live, to raise the retail prices for e-book versions of New Releases and NYT Bestsellers to the caps set by Apple.

Each of the Publisher Defendants realized that its negotiations with Amazon would be difficult, but in their view they had embarked upon a mission that was necessary to protect the publishing business. They took comfort in their knowledge that the five of them stood together, and in Apple's presence in the market. As Reidy wrote to Cue on the day before the iBookstore was officially announced, it was her hope that the iPad Launch "will sustain us as we move through the next steps in this process of changing the industry."

This would not have happened without Apple's ingenuity and persistence. Apple's task had not been easy, but it had succeeded. As Reidy acknowledged in an email to Cue on January 21, working with the Publishers had been like "herding … cats." For his part, Cue appreciated all that Reidy had done to convince her peers to join forces with Apple at several critical junctures. He thanked Reidy for being a "real leader."

The Publisher Defendants took those "next steps" to "chang[e] the industry" immediately; the coordinated pressure on Amazon began at once. On the day of the Launch, January 27, HarperCollins advised Amazon in writing that it had reached its first agency agreement with Apple. "In the interest of 'no surprises,'" HarperCollins advised Amazon that it had decided to move all of their New Release e-books to the agency model, and had "reached an agreement with our first agent, Apple" last night. Penguin also called Amazon on January 27, right after the Launch, to explain that it had moved to agency with its "first customer," referring to Apple.[4746] Macmillan's Sargent did not attend the Launch, because as he had told Cue on January 24, "I expect I will be in Seattle or traveling back," from delivering the news in person to Amazon.[4847]

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[46] Grandinetti responded that he did not understand why Penguin was "working so hard to have [Amazon send it] less money on each sale while at the same time, reducing total sales and frustrating us."

[47] Cue admitted at trial that Apple "expected" each of the Publisher Defendants to demand that Amazon move to an agency model, but denied actually "knowing" that they would. This testimony was not credible, for many reasons. Cue's denial of prior knowledge of Sargent's trip to Amazon was particularly brazen given the January 24 email in which Sargent explained his inability to attend the Launch because he would be traveling to Seattle, Jobs's comment to his biographer on January 28—the day of Sargent's meeting with Amazon—that the Publisher Defendants "went to Amazon and said, 'You're going to sign an agency contract or we're not going to give you the books,'" a January 30 email exchange between Saul and Cue monitoring news about Amazon's decision to remove Macmillan's buy buttons and wondering

L. January 27: The Launch of the iPad and iBookstore

On January 27, Jobs launched the iPad. As part of a beautifully orchestrated presentation, he also introduced the iPad's e-reader capability and the iBookstore. He proudly displayed the names and logos of each Publisher Defendant whose books would populate the iBookstore. To show the ease with which an iTunes customer could buy a book, standing in front of a giant screen displaying his own iPad's screen, Jobs browsed through his iBooks "bookshelf," clicked on the "store" button in the upper corner of his e-book shelf display, watched the shelf seamlessly flip to the iBookstore,[4948] and purchased one of Hachette's NYT Bestsellers, Edward M. Kennedy's memoir, *True Compass*, for $14.99. With one tap, the e-book was downloaded, and its cover appeared on Jobs's bookshelf, ready to be opened and read.

When asked by a reporter later that day why people would pay $14.99 in the iBookstore to purchase an e-book that was selling at Amazon for $9.99, Jobs told a reporter, "Well, that won't be the case." When the reporter sought to clarify, "You mean you won't be 14.99 or they won't be 9.99?" Jobs paused, and with a knowing nod responded, "The price will be the same," and explained that "Publishers are actually withholding their books from Amazon because they are not happy." With that statement, Jobs acknowledged his understanding that the Publisher Defendants would now

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whether Cue had "talk[ed] with [J]on" Sargent and a January 31 email in which Sargent reported to Cue on the trip.

[48] To the public's delight, Jobs described this transition as "like a secret passageway."

wrest control of pricing from Amazon and raise e-book prices, and that Apple would not have to face any competition from Amazon on price.

The import of Jobs's statement was obvious. On January 29, the General Counsel of S&S wrote to Reidy that she "cannot believe that Jobs made the statement" and considered it "[i]ncredibly stupid."

M. January 28 to 31: The Publisher Defendants Force Amazon to Adopt the Agency Distribution Model

As previously discussed, the Publishers recognized that any one of them acting alone would not be able to compel Amazon to move to agency. Five of them had now agreed to join forces, but none of them was eager to be the first to meet with Amazon. As Sargent explained, however, he knew the Apple Agreement gave the Publishers "a point in time when we could actually address our … issues with Amazon"; it "gave us the chance to change the entire business model for digital books." So Sargent made the first move.

Skipping the Launch to which he had been invited, Sargent flew instead to Seattle, accompanied by Napack. Thus, Macmillan, the smallest of the five Publishers, did the honorable thing and delivered its message in person. Sargent did not expect the meeting to go well. As he put it, he was "on [his] way to Seattle to get [his] ass kicked by Amazon." He was right.

At their meeting, Sargent advised Amazon on January 28 that it had just two options: either (1) move to an agency arrangement or (2) not receive Macmillan's Kindle versions of New Releases for seven months. Seven months was no random period—it was the number of months for which titles were designated New

Release titles under the Apple Agreement and restrained by the Apple price caps and MFN. The meeting lasted roughly twenty minutes. Amazon let Macmillan know in blunt terms that it was unhappy.

Macmillan had anticipated that Amazon might retaliate against it by removing the "buy buttons" on the Amazon site that allow customers to purchase books from Amazon's online store or from the Kindle, or by eliminating Macmillan's products from its sites altogether. That night, Macmillan learned which option Amazon had chosen. Amazon removed the buy buttons for both print and Kindle versions of Macmillan titles. Customers could view the Macmillan books on the Amazon website but could not purchase them.

On January 30, Sargent took out an ad in an industry publication to communicate quickly with the industry. Written in the form of a letter to "Macmillan authors/illustrators and the literary agent community," Sargent described the terms he offered to Amazon during their Thursday meeting, including the "deep windowing of titles" if Amazon did not switch to the agency model. He explained that Macmillan would price most titles at first release under the agency model between $12.99 and $14.99. Sargent expressed his regret at Amazon's reaction to his ultimatum, and explained the reasons he had for acting as he did.

> In the ink-on-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 stable and rational. 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.

Macmillan knew it would not stand alone. Sargent wrote to a friend several days later that "the deal that 5 of us did with Apple meant someone was gonna have to do it [first]. … The optics make it look like I stood alone, but in the end I had no doubt that the others would eventually follow."[5049] Hachette's Nourry had written to Sargent the day after the publication of Sargent's letter to the industry stating, "I can ensure you that you are not going to find your company alone in the battle" with Amazon.[5150] The next day, Penguin's Makinson similarly wrote, "[j]ust to say that I'm full of admiration for your articulation of Macmillan's position on this. Bravo." Internally, Hachette's Nourry told Young that he wanted to "enter in the battle as soon as possible," and in an allusion to Macmillan's small size, that he was "thrilled to know how A will react against 3 or 4 of the big guys."

Over the weekend, it became obvious to Amazon that its strategy had failed. The feedback was mixed, but included intense criticism of Amazon by customers and publishers. Nourry celebrated on Monday, Febru-

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[49] Conscious that he should not admit the truth, Sargent disingenuously added: "Interesting in that we did the Apple deal with no contact with other publishers, yet when Jobs announced he had 5 on the agency plan things were clear."

[50] The next day, Nourry wrote a similar email to Sargent's superior, Stefan von Holtzbrinck, assuring him that he "very much appreciate[s] what MacMillan is doing" and he can "[b]e sure others will enter the battle field!"

ary 1, by observing that “Amazon’s stock is down 9%!”[5251]

Amazon knew that its battle was not just with Macmillan but with five of the Big Six. As Grandinetti testified, “[i]f it had been only Macmillan demanding agency, we would not have negotiated an agency contract with them. But having heard the same demand for agency terms coming from all the publishers in such close proximity … we really had no choice but to negotiate the best agency contracts we could with these five publishers.” Unless it moved to an agency distribution model for e-books, Amazon customers would cease to have access to many of the most popular e-books, which would hurt Kindle customers and the attractiveness of the Kindle.

Amazon announced on its website on Sunday, January 31, that it would “capitulate and accept” Macmillan’s agency terms “because Macmillan has a monopoly over their own titles, and we will want to offer them to you even at prices we believe are needlessly high for e-books.” Shortly thereafter, Amazon sent a letter to the Federal Trade Commission complaining about the simultaneous nature of the demands for agency from the Publishers who had signed with Apple.

N. The Five Amazon Agency Agreements

On Sunday, January 31, Amazon signaled to Macmillan that it was willing to negotiate. That night, Sargent sent an e-mail marked “URGENT!!” to Cue. Sargent explained that he was “gonna need to figure out our final agency terms of sale tonight. Can you call me

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[51] The subject line of the email was “Now it must really hurt …”.

please?" Cue and Sargent spoke that night.[5352] With help from Apple, Macmillan negotiated an agency agreement with Amazon, which was signed that Friday, February 5.

Macmillan made no secret of its intention to raise prices. Sargent wrote to Grandinetti on February 2, that "[w]e can not budge on the final price that the consumers pay for our books. … That is the very heart of the agency model, and it is why we are doing this. … [W]e can not give up control of price. If we do we are much worse off than we were before." But, referring to Macmillan's across-the-board shift to agency, Sargent assured Amazon that it "will never be disadvantaged on [the] pricing" for Macmillan's e-books.

In light of their overlapping threats to remove content from Amazon's platform if it did not move to agency in early April, when the iPad became available, Amazon moved quickly to execute agency agreements with the remaining Publisher Defendants. But, to avoid being vulnerable in the future to collective pressure during contract negotiations, Amazon insisted that each of the five agency agreements have a different termination date. The final five contracts ranged in length from terms of eighteen months to three years, or ended on different dates, from January 31, 2012 to June 30, 2012.

Amazon did not want to give up control over pricing or raise its prices, and like Apple, assumed that under an agency model each of the Publisher Defendants

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[52] While Cue denied at trial that their conversation was about the Macmillan negotiations with Amazon, his denial was not credible. Macmillan had executed its Agreement with Apple a week earlier; the only final agency terms still under discussion were with Amazon.

would set retail prices at the price caps. During the negotiations, therefore, it shared data with the Publisher Defendants illustrating how the wholesale model was more profitable for the Publishers. Amazon also included a "model parity" clause in any agreement. This gave Amazon the option to return to a wholesale model of distribution in the event any Publisher agreed to a wholesale distribution arrangement with any other e-tailer.

During their negotiations with Amazon, the Publisher Defendants shared their progress with one another. As Naggar testified, whenever Amazon "would make a concession on an important deal point," it would "come back to us from another publisher asking for the same thing or proposing similar language." For example, when Amazon agreed with one Publisher Defendant to forego any promotional activity in exchange for assurance that it would never be disadvantaged on price, it received a call the next day from another saying, "so I understand … you're willing to forego promotions." Similarly, with respect to the length of the agreements, Penguin's McCall left a voicemail for Naggar indicating that Penguin had been "hearing through the grapevine that you guys are maybe coming to some agreements that are less than three years … maybe you're moving off of that," and suggesting they chat.

By the end of March 2010, Amazon had completed agency agreements with Macmillan, HarperCollins, Hachette, and S&S. Because of circumstances that were unique to Penguin and its reseller contract, its agency agreement with Amazon was the last to be executed. Penguin signed its agency contract with Amazon on June 2, 2010, but before that date, Penguin had refused to allow Amazon to sell any of Penguin's new e-books.

Apple closely monitored the progress of the Publisher Defendants in their negotiations with zon.[5453] The Publisher Defendants told Apple when their agency agreements with Amazon had been signed, and Apple watched as they swiftly moved their prices for New Release e-books on Amazon to the top of Apple's tiers. On April 3, 2010, Cue emailed Jobs to report that "[w]e have reviewed all the books on Amazon and they have switched to agency with the publishers. … Overall, our NYT bestsellers and new releases are the same as Amazon." At that point, Penguin was the only Publisher Defendant who had not yet signed an agency agreement with Amazon. As such, Cue told Jobs that Apple was "changing a bunch of Penguin titles to $9.99 … because they didn't get their Amazon deal done." When Penguin's Shanks wrote to Cue to share the news it had "finally" reached an agreement with Amazon "on our new terms of sale," he added that "The playing field is now level." Cue responded, "Great news and congratulations!!!"

O. Prices after Agency

Just as Apple expected, after the iBookstore opened in April 2010, the price caps in the Agreements became the new retail prices for the Publisher Defendants' e-books. In the five months that followed, 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

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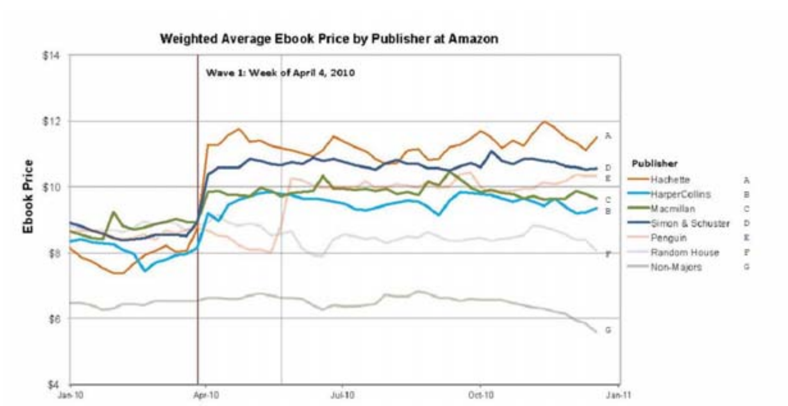
[53] At trial, Moerer at first denied that he had watched the prices of the Publisher Defendants' e-books on Amazon or had noticed that they had increased to the price caps. As a director of iTunes for Apple, this was not credible, and Apple witnesses, included Moerer, eventually came to admit that they did track these price increases as they were occurring.

within 1% 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. The increases at Amazon within roughly two weeks of moving to agency amounted to an average per unit e-book retail price increase of 14.2% for their New Releases, 42.7% for their NYT Bestsellers, and 18.6% across all of the Publisher Defendants' e-books.

The following chart, prepared by one of Apple's experts, illustrates this sudden and uniform price increase. While the average prices for Random House's e-books hovered steadily around $8, for four of the Publisher Defendants, the price increases occurred at the opening of the iBookstore; Penguin's price increases awaited the execution of its agency agreement with Amazon and followed within a few weeks. The bottom flat line represents the average prices of non-major publishers.



The Publisher Defendants raised more than the prices of just New Release e-books. The prices of some of their New Release *hardcover* books were also raised in order to move the e-book version into a correspondingly higher price tier.[5554] And, all of the Publisher Defendants raised the prices of their backlist e-books, which were not governed by the Agreements' price tier regimen. As Cue had anticipated, the Publisher Defendants did this in order to make up for some of the revenue lost from their sales of New Release e-books.

The following two charts, one prepared by the Plaintiffs' expert and another from an expert for Apple, respectively, compare the price increases for the Publisher Defendants' New Releases with the price increases for their backlist books. Despite drawing from different time periods, their conclusions are very similar. The Publisher Defendants used the change to an agency method for distributing their e-books as an opportunity to raise the prices for their e-books across the board.

E-Book Average Price Increases at Amazon by Publisher Defendants Following the Move to Agency

Amazon Weighted Average Price Increases

Publisher	All eBooks	New Releases	NYT Bestsellers	Backlist
Hachette	33.0%	14.1%	37.9%	37.5%
HarperCollins	13.6%	12.5%	44.0%	15.2%
Macmillan	11.6%	14.0%	-	11.2%
Penguin	18.3%	19.5%	43.6%	17.6%
Simon & Schuster	18.0%	15.1%	28.7%	19.8%
Defendant Publishers	18.6%	14.2%	42.7%	19.6%
Random House	0.01%	1.9%	0.2%	0.3%
Non-Majors	-0.2%	-0.9%	1.1%	0.1%

[54] The relationship between the price of e-books and their hardcover counterpart is a complex topic that was only tangentially explored at trial. Apple conceded, however, that it had not been Amazon's policy to price e-books above their hardcover version, but that the Publishers who adopted an agency model for distribution of their e-books did not always follow that practice. There is evidence that, with the adoption of the agency model, as many as 20% of trade e-books became more expensive for consumers than their physical counterpart.

Average E-book Prices of Backlist and New Release Titles in the Periods Before and After Agency

	Amazon	Barnes & Noble	Sony
Backlist			
Before Agency	$7.16	$6.84	$8.07
After Agency	$8.78	$8.20	$8.43
Percent Change	23%	20%	4%
Hardcover New Release and NYT Bestsellers			
Before Agency	$10.37	$9.99	$11.31
After Agency	$12.28	$11.60	$11.97
Percent Change	18%	16%	6%

Not surprisingly, the laws 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.

There were various measurements offered at trial to quantify the lost sales. One study found that the Publisher Defendants who shifted their e-tailers to agency in early April 2010 sold 12.9% fewer units at major retailers in a two-week period following the implementation of agency prices than they had in a two-week period preceding it, at least for books that were available in both periods.[5655] Another expert opined that the Publisher Defendants' sales decreased by 14.5% relative to a control group consisting of Random House.[5756]

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[55] By contrast, in this study non-party publishers' sales increased 5.4% in the same period.

[56] Apple argued at trial that the decline in sales of the Publisher Defendants' e-books compared to those sold by Random House was attributable to Amazon's promotion of Random House books during the time Random House remained on a wholesale model of distribution. Apple did not offer persuasive evidence, however, that the loss in sales was substantially due to anything other than the fact that Amazon continued to price many Random

Amazon prepared charts for the Publisher Defendants illustrating the impact of their pricing decisions on their sales. Amazon concluded that "[c]ompared to the 3 agency publishers—Harper, Hachette and Penguin, who had overall kindle book units decline in Q2 compared to Q1, Random House had an increase of 41%." It is unnecessary to quantify the precise decline in the sales for the Publisher Defendants that can be properly attributed to their decisions to raise their e-book prices. It is abundantly clear, and not surprising, that each of the Publisher Defendants lost sales of e-books due to the price increases.

Thus, consumers suffered in a variety of ways from this scheme to eliminate retail price competition and to raise e-book prices. Some consumers had to pay more for e-books; others bought a cheaper e-book rather than the one they preferred to purchase; and it can be assumed that still others deferred a purchase altogether rather than pay the higher price. Now that the Publisher Defendants were in control of pricing, they were also less willing to authorize retailers to give consumers the benefit of promotions. As Macmillan explained to Barnes & Noble, it would not agree to a proposed promotion because "[w]e worked hard to push the price of our new Ebooks up just a few dollars—and this would immediately signal not an increase in value, but a decrease in value."

While conceding that the prices for the Publisher Defendants' e-books went up after Apple opened the iBookstore, Apple argued at trial that the opening of the iBookstore actually led to an overall decline in trade e-book prices during the two-year period that followed

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House New Releases at $9.99 while the Publisher Defendants raised the prices of their e-books substantially higher.

that event. Its evidence was not persuasive. Apple's experts did not present any analysis that attempted to control for the many changes that the e-book market was experiencing during these early years of its growth, including the phenomenon of disintermediation and the extent to which other publishers decided to remain on the wholesale model. The analysis presented by the Plaintiffs' experts as well as common sense lead invariably to a finding that the actions taken by Apple and the Publisher Defendants led to an increase in the price of e-books. After all, the Publisher Defendants accounted for roughly 50% of the trade e-book market in April 2010, and it is undisputed that they raised the prices for not only their New Release but also their backlist e-books substantially.

P. Random House Adopts an Agency Model

If there were any doubt about the impact of the Apple agency Agreement on e-book prices, at least in so far as the market for trade e-books is concerned, the experience of Random House confirms each of the observations just made about the prices and sales of the five Publisher Defendants. Random House adopted the agency model in early 2011, and promptly raised the prices of its e-books and experienced a concomitant decline in e-book sales.[5857]

Random House had resisted Apple's overtures to adopt the agency model and therefore its e-books were not available in 2010 in the iBookstore. It was Cue's assessment that the iBookstore was not as successful as Apple had hoped because e-books from Random House,

[57] Dr. Ashenfelter calculated an increase in Random House's prices for e-books of 18.3% on average, and a decrease in its unit sales of e-books of 16.7%.

the largest of the Big Six, were not being sold there. Cue believes that consumers expect all the books they may want to buy to be available in a bookstore and when they cannot find what they want, they go elsewhere and may never return.

While the Publisher Defendants were pricing their e-books at or close to the $12.99 and $14.99 price caps, Amazon continued to price many Random House New Releases and NYT Bestseller e-books at $9.99, as it did with other publishers that remained on its wholesale terms. This increased Random House's sales and market share during that period.

Apple decided to pressure Random House to join the iBookstore. As Cue wrote to Apple CEO Tim Cook, "when we get Random House, it will be over for everyone." Apple had its opportunity in the Fall of 2010, when Random House submitted some e-book apps to Apple's App Store. Cue advised Random House that Apple was only interested in doing "an overall deal" with Random House. By December, they had begun negotiations, and Random House executed an agency agreement with Apple in mid-January 2011. In an email to Jobs, Cue attributed Random House's capitulation in part to "the fact that I prevented an app from Random House from going live in the app store this week."

Q. The Publisher Defendants Require Google to Adopt an Agency Model

The decision by the Publisher Defendants and later by Random House to adopt the agency model of distribution and raise e-book prices effected a change across the entire industry. Once the Publisher Defendants agreed with Apple to move to an agency relationship for the sale of their e-books, they not only demanded that Amazon change their relationship to an agency model, they negotiated agency agreements with their other e-book distributors to eliminate all retail price competition.

One of the companies that was planning to become an e-book distributor was Google, and the Publisher Defendants demanded that Google as well adopt an agency agreement in January 2010. Google had begun to plan its entry into the e-book business as early as 2007. Before January 2010, Google understood from its discussions with the Publisher Defendants that the parties would use the wholesale model to sell digital books. But, in January 2010, each of the Publisher Defendants did an about-face and suddenly advised Google that they were switching to an agency model and would no longer be offering books under wholesale terms. Google, like Amazon, would have preferred to use the wholesale model and set the retail prices for its e-books, but the Publisher Defendants refused to allow it that option. The Publisher Defendants conveyed to Google that their Agreements with Apple made them "unwilling to enter into non-agency agreements with Google."

R. Concluding Observations

While many of the trial's fact witnesses who are employed by Apple and the Publisher Defendants were less than forthcoming, the contemporaneous documentary record was replete with admissions about their scheme. The preceding findings have therefore come not only from the testimony presented at trial, where the witnesses were cross-examined and questioned again through re-direct examination, but has also been derived liberally from the documentary record.

Based on these documents, it is difficult for either Apple or the Publisher Defendants to deny that they worked together to achieve the twin aims of eliminating retail price competition and raising the prices for trade e-books. As Macmillan frankly acknowledged in writing to the trade in the Spring of 2010, one of its goals in moving to the agency model was to "[i]ncrease[e] prices" of e-books. As Penguin's McCall wrote, "Agency is anti-pricewar territory. We don't need to compete with other publishers on the price of our books." Penguin executives told authors after signing the Apple Agreement that they had "fought to protect high prices; … fought against $9.99 pricing" to demand higher, "better" prices. It continued, "who knows, it is $14.99 this year, but in a few years it may be $16.99 or $19.99." HarperCollins recognized that, with the Apple Agreements, Apple had become the "gatekeeper" on e-book pricing "for the industry." As Cue admitted at trial, raising e-book prices was simply "all part of" the bargain in creating the iBookstore.

Jobs himself was frank in explaining how this scheme worked when he spoke to biographer Walter Isaacson the day after the Launch. Jobs described it as an "a[i]kido move" to move all retailers to agency and eliminate price competition with Amazon. In Jobs's own words:

> Amazon screwed it up. It paid the wholesale price for some books, but started selling them below cost at $9.99. The publishers hated that—they thought it would trash their ability to sell hardcover books at $28. So before Apple even got on the scene, some booksellers were starting to withhold books from Amazon. So we told the publishers, "We'll go to the agency model, where you set the price, and we get our 30%, and yes, the customer pays a little more, but that's what you want anyway." But we also asked for a guarantee that if anybody else is

> selling the books cheaper than we are, then we can sell them at the lower price too. So they went to Amazon and said, "You're going to sign an agency contract or we're not going to give you the books."

DISCUSSION

The United States of America has brought a single claim against Apple for violation of Section 1 of the Sherman Act. The States have brought claims against Apple based on violations of the state statutes "to the extent those laws are congruent with Section 1 of the Sherman Act." Following a description of the legal standard for a Section 1 claim, this Opinion will apply that law to the facts presented at trial. After finding that the Plaintiffs' have carried their burden of showing that Apple violated Section 1, the Opinion will address the six principal arguments that Apple has presented in its defense.

A. Legal Standard

Section 1 of the Sherman Act ("Section 1") outlaws "[e]very contract, combination … , or conspiracy, in restraint of trade or commerce among the several States." 15 U.S.C. § 1. To establish a conspiracy in violation of Section 1, then, proof of joint or concerted action is required. *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 761 (1984). In particular, plaintiffs must show (1) "a combination or some form of concerted action between at least two legally distinct economic entities" that, (2) "constituted an unreasonable restraint of trade either per se or under the rule of reason." *Primetime 24 Joint Venture v. Nat'l Broad. Co.*, 219 F.3d 92, 103 (2d Cir. 2000) (citation omitted); *see Capital Imaging Assocs, P.C. v. Mohawk Valley Medical Assocs, Inc.*, 996 F.2d 537, 542 (2d Cir. 1993). Overall, "[c]ircumstances must reveal a unity of purpose or a common design and understanding, or a meeting of minds in an unlawful arrangement." *Monsanto*, 465 U.S. at 764 (citation omitted); *Apex Oil Co. v. DiMauro*, 822 F.2d 246, 252 (2d Cir. 1987).

Notwithstanding its broad language, Section 1 does not disallow any and all agreements; it "outlaws only unreasonable restraints." *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 885 (2007) (citation omitted). Thus, in many cases, "antitrust plaintiffs must demonstrate that a particular contract or combination is in fact unreasonable and anticompetitive before it will be found unlawful." *Texaco Inc. v. Dagher*, 547 U.S. 1, 5 (2006). Some agreements, however, "are so plainly anticompetitive that no elaborate study of the industry is needed to establish their illegality." *Id.* (citation omitted). Such agreements are illegal *per se*, and are not subject to the rule of reason. The *per se* rule thus "eliminates the need to study the reasonableness of an individual restraint in light of the real market forces at work." *Leegin*, 551 U.S. at 886.

By contrast, under the rule of reason, "the plaintiffs bear an initial burden to demonstrate the defendants' challenged behavior had an actual adverse effect on competition as a whole in the relevant market." *Geneva Pharms Tech Corp. v. Barr Labs Inc.*, 386 F.3d 485, 506-07 (2d Cir. 2004) (citation omitted).

> If the plaintiffs satisfy their initial burden, the burden shifts to the defendants to offer evidence of the pro-competitive effects of their agreement. Assuming defendants can provide such proof, the burden shifts back to the plaintiffs to prove that any legitimate competitive benefits offered by defendants could have been

> achieved through less restrictive means. Ultimately, the fact finder must engage in a careful weighing of the competitive effects of the agreement—both pro and con—to determine if the effects of the challenged restraint tend to promote or destroy competition.

Id. at 507 (citation omitted).

Use of the *per se* rule is limited to restraints "that would always or almost always tend to restrict competition and decrease output," and is appropriate "only after courts have had considerable experience with the type of restraint at issue." *Leegin*, 551 U.S. at 886 (citation omitted). "Under the Sherman Act a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal *per se*." *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 223 (1940). Generally speaking, price-fixing agreements or agreements to divide markets that are horizontal in nature—meaning that the parties to the agreement are "competitors at the same level of the market structure," *Anderson News, L.L.C. v. American Media, Inc.*, 680 F.3d 162, 182 (2d Cir. 2012) (citation omitted)—are *per se* unlawful. *Starr v. Sony BMG Music Entm't*, 592 F.3d 314, 326 n.4 (2d Cir. 2010); *Leegin*, 551 U.S. at 886 ("Restraints that are *per se* unlawful include horizontal agreements among competitors to fix prices."). In other words, "they are prohibited despite the reasonableness of the particular prices agreed upon." *Starr*, 592 F.3d at 326 n.4. Non-price restrictions that are otherwise lawful are also "per se unlawful if undertaken as part of an illegal scheme to fix prices." *Monsanto*, 465 U.S. at 760 n.6 (citation and emphasis omitted).

By contrast, vertical price restraints, such as resale price maintenance agreements, that do not involve price-fixing are subject to the rule of reason. *See Leegin*, 551 U.S. at 882. A manufacturer has a right to refuse to deal "with whomever it likes, as long as it does so independently." *Monsanto*, 465 U.S. at 761.

A plaintiff may rely on either direct or circumstantial evidence to establish that a defendant entered into an agreement in violation of the antitrust laws. *Mayor and City Council of Baltimore, Md. v. Citigroup, Inc.*, 709 F.3d 129, 136 (2d Cir. 2013) (pleading standard). Direct evidence "would consist, for example, of a recorded phone call in which two competitors agreed to fix prices at a certain level." *Id.*

Because unlawful conspiracies tend to form in secret, however, proof of a conspiracy will rarely consist of explicit agreements. Rather, conspiracies "nearly always must be proven through inferences that may fairly be drawn from the behavior of the alleged conspirators." *Anderson News*, 680 F.3d at 183 (citation omitted). In fact, even direct evidence in antitrust cases "can sometimes require a factfinder to draw inferences to reach a particular conclusion." *In re Publ'n Paper Antitrust Litig.*, 690 F.3d 51, 64 (2d Cir. 2012) ("Perhaps on average circumstantial evidence requires a longer chain of inferences." (citation omitted)). Circumstantial evidence is no less persuasive than direct evidence; indeed, "[c]ircumstantial evidence is not only sufficient, but may also be more certain, satisfying and persuasive than direct evidence." *Desert Palace, Inc. v. Costa*, 539 U.S. 90, 100 (2003).

Thus, to prove an antitrust conspiracy, "the antitrust plaintiff should present direct or circumstantial evidence that reasonably tends to prove that the [defendant] and others had a conscious commitment to a common scheme designed to achieve an unlawful objective." *Monsanto*, 465 U.S. at 764 (citation omitted). The evidence must also "prove defendants had the intent to adhere to an agreement that was designed to achieve an unlawful objective; specific intent to restrain trade is not required." *Geneva Pharms*, 386 F.3d at 507. Since "the essence of any violation of § 1 [of the Sherman Act] is the illegal agreement itself," *Summit Health, Ltd. v. Pinhas*, 500 U.S. 322, 330 (1991), the evidence must demonstrate a "meeting of the minds." *Monsanto*, 465 U.S. at 765. In evaluating the existence of an antitrust conspiracy, courts consider the "totality of the evidence." *Publ'n Paper*, 690 F.3d at 64; *see Cont'l Ore Co. v. Union Carbide & Carbon Corp.*, 370 U.S. 690, 699 (1962) ("The character and effect of a conspiracy are not to be judged by dismembering it and viewing its separate parts, but only by looking at it as a whole." (citation omitted)). Just as a conspiracy's "failure to achieve its ends" after an intended period may be "strong evidence" that the conspiracy did not in fact exist, *Matsushita Electric Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 592 (1986), the success of the conspiracy in achieving its goals may confirm the very existence of the conspiracy. *See Oreck Corp. v. Whirlpool Corp.*, 563 F.2d 54, 63 (2d Cir. 1977) ("Proof that a combination was formed for the purpose of fixing prices and that it caused them to be fixed or contributed to that result is proof of the completion of a price-fixing conspiracy under § 1 of the Act." (citation omitted)); *cf. United States v. Quinones*, 511 F.3d 289, 308 (2d Cir. 2007) (defendants' cocaine purchases "were obviously relevant to proof of the existence of th[e narcotics] conspiracy" charged).

"*Unambiguous* evidence of an agreement to fix prices … is all the proof a plaintiff needs" to establish a violation of Section 1. *Publ'n Paper*, 690 F.3d at 63 (citation omitted). Where the evidence of conspiracy is "ambiguous," however, "antitrust law limits the range of permissible inferences" that may be drawn. *Matsushita*, 475 U.S. at 588; *see Apex*, 822 F.2d at 253. Where conduct is as consistent with permissible competition as with illegality, a plaintiff "must present evidence that tends to exclude the possibility that the alleged conspirators acted independently." *Matsushita*, 475 U.S. at 588 (citation omitted). Thus, "standing alone," ambiguous conduct is inadequate to support an inference of illegality. *Id.* Moreover, where a plaintiff's theory of recovery is implausible—in other words, "if the claim is one that simply makes no economic sense," *id.* at 587—it takes "strong direct or circumstantial evidence to satisfy Matsushita's tends to exclude standard." *Publ'n Paper*, 690 F.3d at 63 (citation omitted). "By contrast, broader inferences are permitted, and the 'tends to exclude' standard is more easily satisfied, when the conspiracy is economically sensible for the alleged conspirators to undertake and the challenged activities could not reasonably be perceived as procompetitive." *Id.* (citation omitted).

Even where a plaintiff relies on ambiguous evidence, however, to prove its claim, the plaintiff does not bear the burden of showing that the existence of a conspiracy is the "*sole* inference" to be drawn from the evidence. *Id.* The plaintiff is only required to present evidence that is sufficient to allow the fact-finder "to infer that the conspiratorial explanation is more likely than not." *Id.* (citation omitted).

Conduct that stems from independent decisions is permissible under Section 1, *see Starr*, 592 F.3d at 321, as are "independent responses to common stimuli," and "interdependence unaided by an advance understanding among the parties." *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 556 n.4 (2007) (citation omitted). As a result, while evidence of parallel conduct is probative of an antitrust conspiracy, such evidence "alone cannot suffice." *Apex*, 822 F.2d at 252; *Matsushita*, 475 U.S. at 588. Instead, to infer a horizontal agreement through parallel conduct, a court may draw inferences from "plus factors" to rule out purely interdependent decision making by rivals. *Mayor*, 709 F.3d at 136 (citation omitted). Plus factors commonly considered by courts include "a common motive to conspire, evidence that shows that the parallel acts were against the apparent individual economic self-interest of the alleged conspirators, … evidence of a high level of interfirm communications," *id.*, and the "use of facilitating practices" like information sharing. *Todd v. Exxon Corp.*, 275 F.3d 191, 198 (2d Cir. 2001). An abrupt shift from defendants' past behavior and near-unanimity of action by several defendants may also strengthen the inference. *See Interstate Circuit v. United States*, 306 U.S. 208, 222 (1939); *Toys "R" Us, Inc. v. FTC*, 221 F.3d 928, 935 (7th Cir. 2000). For instance, a "complex and historically unprecedented change[] in pricing structure made at the very same time by multiple competitors, and made for no other discernible reason," may provide sufficient evidence of an illegal conspiracy. *Mayor*, 709 F.3d at 137 (citation omitted) (discussion of pleading standard).

Per se price-fixing agreements may also include those where a vertical player participates in and facilitates a horizontal conspiracy. *See Toys "R" Us*, 221 F.3d at 934, 936. Where a vertical actor is alleged to have participated in an unlawful horizontal agreement, plaintiffs must demonstrate both that a horizontal conspiracy existed, and that the vertical player was a knowing participant in that agreement and facilitated the scheme. *See, e.g.*, *id*. at 936; *Interstate Circuit*, 306 U.S. at 225-29 (1939).

B. Analysis of the Evidence

The Plaintiffs have shown through compelling evidence that Apple violated Section 1 of the Sherman Act by conspiring with the Publisher Defendants to eliminate retail price competition and to raise e-book prices. There is overwhelming evidence that the Publisher Defendants joined with each other in a horizontal price-fixing conspiracy. Through that conspiracy, the Publisher Defendants raised the prices of many of their New Releases and NYT Bestsellers above the $9.99 price at which they had previously been sold through Amazon. They also raised the prices of many of their backlist e-books. The Plaintiffs have also shown that Apple was a knowing and active member of that conspiracy. Apple not only willingly joined the conspiracy, but also forcefully facilitated it.

There is little dispute that the Publisher Defendants conspired together to raise the prices of their e-books.[58] They shared a common motivation: the elimination of the "wretched" $9.99 retail price that Amazon, the chief distributor of their e-books, chose for many of their New Releases, including NYT Bestsellers. They believed that this price point in the nascent but swiftly growing e-book market would, if left unchallenged, unalterably affect the consumer perception of the value of a book and

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[58] During summation Apple chose not to concede that the plaintiffs had proven at trial that the Publisher Defendants engaged in a horizontal price fixing conspiracy. Apple did not expend an effort, however, to argue that such a conspiracy did not exist or that the evidence was insufficient to find that it existed. Apple confined its argument to its purported lack of knowledge that the Publisher Defendants were conspiring with each other.

severely undermine their more profitable physical book business. To protect their then-existing business model, the Publisher Defendants agreed to raise the prices of e-books by taking control of retail pricing.

From late 2008 through 2009, the Publisher Defendants had collectively tried through a variety of means to pressure Amazon to raise the prices of their e-books. Their efforts proved futile. Then, through agency agreements that each Publisher Defendant executed with Apple over the course of just three days in January 2010, and with Amazon (and other e-retailers) in the weeks that followed, the Publisher Defendants simultaneously switched from a wholesale to an agency model for the distribution of their e-books. When the iPad went on sale and the iBookstore went live in early April 2010 (or shortly thereafter, in the case of Penguin), each of the Publisher Defendants used their new pricing authority to raise the prices of their e-books overnight and substantially.

This price-fixing conspiracy would not have succeeded without the active facilitation and encouragement of Apple. Before Apple even met with the Publisher Defendants in mid-December 2009, it was fully aware that the Publishers were adamantly opposed to Amazon's $9.99 price point and were actively searching for an effective means, including through collective action, to pressure Amazon to raise its prices. Inspired by the impending Launch of the revolutionary iPad, scheduled for January 27, Apple seized the moment.

Apple met with the Publishers in December 2009 and heard their unanimous condemnation of the $9.99 price point and desire to raise e-book prices. Volunteering that it was willing to price e-books as high as $14.99 in an e-bookstore, Apple won their rapt attention. Apple then presented a strategy—the agency Agreements—that would allow the Publishers to take control of and raise e-book retail prices in a matter of weeks. Knowing full well, however, that the Publisher Defendants wanted to raise e-book retail prices significantly above the $9.99 price point, even in some instances above the retail prices of the corresponding physical book, Apple placed pricing restrictions or caps on categories of e-books to ensure that the prices in its iBookstore were "realistic" and didn't embarrass Apple. In negotiating the caps for its pricing tiers, Apple understood that it was setting the new retail prices at which e-books would be sold.

Apple had several reasons for engaging as it did with the Publisher Defendants. It wanted to announce a well-stocked iBookstore in less than two months, when it launched its iPad; it wanted to avoid competing with Amazon, an arch rival in the market, on the basis of price; and it wanted a guaranteed profit on any new business it entered. To accomplish these goals, Apple was willing to offer the Publisher Defendants a roadmap for raising retail e-book prices well above Amazon's $9.99 price point and urged the Publisher Defendants to use that roadmap to do so. In short, Apple convinced the Publisher Defendants that Apple shared their goal of raising e-book prices, and helped them to realize that goal.

Apple included the MFN, or price parity provision, in its Agreements both to protect itself against any retail price competition and to ensure that it had no retail price competition. Apple fully understood and intended that the MFN would lead the Publisher Defendants inexorably to demand that Amazon switch to an agency relationship with each of them. As Apple's Cue reminded Macmillan's Sargent, this was no more than what the Publisher Defendants had already assured Apple that they wanted to, and would, do.

Because of the MFN, Apple concluded that it did not need to include as an explicit term in its Agreements a demand that a Publisher Defendant move all of its resellers to agency. The MFN was sufficient to force the change in model. The economics of the Agreements were, simply put, "terrible" for the Publishers. The Publisher Defendants already expected to lose revenue from their substitution of an agency model for the wholesale model of e-book distribution. Unless a Publisher Defendant followed through and transformed its relationships with Amazon and other resellers into an agency relationship, it would be in significantly worse terms financially as a result of its agency contract with Apple. As significantly, unless the Publisher Defendants joined forces and together forced Amazon onto the agency model, their expected loss of revenue would not be offset by the achievement of their ultimate goal: the protection of book value.

A chief stumbling block to raising e-book prices was the Publishers' fear that Amazon would retaliate against any Publisher who pressured it to raise prices. Each of them could also expect to lose substantial sales if they unilaterally raised the prices of their own e-books and none of their competitors followed suit. This is where Apple's participation in the conspiracy proved essential. It assured each Publisher Defendant that it would only move forward if a critical mass of the major publishing houses agreed to its agency terms. It promised each Publisher Defendant that it was getting identical terms in its Agreement in every material way. It kept each Publisher Defendant apprised of how many others had agreed to execute Apple's Agreements. As Cue acknowledged at trial, "I just wanted to assure them that they weren't going to be alone, so that I would take the fear awa[y] of the Amazon retribution that they were all afraid of." As a result, the Publisher Defendants understood that each of them shared the same set of risks and rewards.

Working against its own internal deadline, Apple achieved for this industry in a matter of weeks what the Publisher Defendants had been unable to accomplish for months before Apple became their partner. In the words of Simon & Schuster's Reidy, Apple herded cats. Apple gave the Publishers a deadline and required them to examine with care but quickly how committed they were to challenging Amazon and altering the landscape of e-book pricing. And when it appeared a Publisher Defendant might be too scared to commit to this dramatic business change, Cue reminded that Publisher Defendant that Apple's entry into the market represented a once-in-a-lifetime opportunity to eliminate Amazon's control over pricing. As he warned Penguin just days before the Launch, "There is no one outside of us that can do this for you. If we miss this opportunity, it will likely never come again."

Without the collective action that Apple nurtured, it is unlikely any individual Publisher would have succeeded in unilaterally imposing an agency relationship on Amazon. Working together, and equipped with Apple's agency Agreements, Apple and the Publisher Defendants moved the largest publishers of trade e-books and their distributors from a wholesale to agency model, eliminated retail price competition, and raised e-book prices.

The evidence of this conspiracy can be found in Jobs's admissions to a reporter, to James Murdoch, and to his biographer; in contemporaneous e-mails pulled from the files of Apple, the Publishers, Amazon, and others; in the web of telephone calls among Publisher Defendants' CEOs surrounding each turning point in the presentation and execution of the Agreements;[59] and as compellingly, in the circumstantial evidence. This circumstantial evidence includes the following: each of the Publisher Defendants shared the identical goal to raise the $9.99 price point to protect its physical book business; the agency Agreements represented an "abrupt shift" from the past model for the distribution of e-books; the Publisher Defendants each demanded that Amazon adopt this new model within days of each other; the agency model protected Apple from price competition; the rise in trade e-book prices to or close to the price caps established in the Agreements was large and essentially simultaneous; in adopting a model that deprived each of them of a stream of expected rev-

[59] Apple has contended that the existence of any conversations among the Publisher Defendants CEOs during their negotiations with Apple is neither unusual nor incriminating. This is not the occasion to describe the metes and bounds of lawful communication among competitors when they are engaged in simultaneous negotiations with either a common supplier or a shared distributor. Instead, the Court focuses here on the ways in which the Publisher Defendants' frequent discussions are relevant to this Opinion, including that the Publisher Defendants' denials at trial that they discussed the Apple Agreement with one another in those communications, or that those conversations occurred at all, in the face of overwhelming evidence to the contrary, strongly supports a finding of consciousness of guilt. They knew they were coordinating their efforts to raise the e-book prices and jointly confront Amazon, and have tried to hide that fact. Moreover, the pattern of their coordination in meetings and telephone calls, and their expectation that they would not compete on price—all of which was apparently well established before Apple reached out to them but continued throughout their negotiations with Apple—serves as strong evidence of this conspiracy.

enue from the sale of e-books on the wholesale model, the Publisher Defendants all acted against their near-term financial interests; and each of the Publisher Defendants acted in identical ways even though each was also afraid of retaliation by Amazon. *See Toys "R" Us*, 221 F.3d at 935-36; *PepsiCo, Inc. v. Coca-Cola Co.*, 315 F.3d 101, 110 (2d Cir. 2002).

In sum, the Plaintiffs have shown not just by a preponderance of the evidence, *see Herman & MacLean v. Huddleston*, 459 U.S. 375, 390 (1983), but through compelling direct and circumstantial evidence that Apple participated in and facilitated a horizontal price-fixing conspiracy. As a result, they have proven a *per se* violation of the Sherman Act. *See Arizona v. Maricopa Cnty. Med. Soc.*, 457 U.S. 332, 346-47 (1982); *Toys "R" Us*, 221 F.3d at 936. If it were necessary to analyze this evidence under the rule of reason, however, the Plaintiffs would also prevail.

Apple has not shown that the execution of the Agreements had any pro-competitive effects.[60] The form Agreements eliminated retail price competition, and there is no evidence that the Publisher Defendants have ever competed with each other on price. To the contrary, several of the Publishers' CEOs explained that they have not competed with each other on that basis. The pro-competitive effects to which Apple has pointed, including its launch of the iBookstore, the technical novelties of the iPad, and the evolution of digital publishing more generally, are phenomena that are independent of the Agreements and therefore do not demonstrate any pro-competitive effects flowing from the Agreements.

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[60] Plaintiffs have defined the relevant market as trade e-books in the United States; Apple does not dispute that characterization.

In any event, the Plaintiffs have shown that the Agreements did not promote competition, but destroyed it. The Agreements compelled the Publisher Defendants to move Amazon and other retailers to an agency model for the distribution of e-books, removed the ability of retailers to set the prices of their e-books and compete with each other on price, relieved Apple of the need to compete on price, and allowed the Publisher Defendants to raise the prices for their e-books, which they promptly did on both New Releases and NYT Bestsellers, as well as backlist titles. Apple's experts did little to counter the evidence of this across-the-board price increase in e-books sold by the Publisher Defendants and by Random House when it moved to agency.[61] Because of this rise in prices, and at least until Random House also adopted the agency model, the Publisher Defendants sold fewer e-books than they otherwise would have done. For this and many other reasons, if it were necessary to evaluate Apple's conduct under the rule of reason, Plaintiffs have carried their burden to show a violation of Section 1 of the Sherman Act under that test as well.

APPLE'S ARGUMENTS

Apple vigorously contested its liability at trial. This Opinion turns now to Apple's principal arguments in its defense.

Apple's defense has somewhat shifted over time. Apple in its opening statement identified five essential

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[61] The testimony by Apple's experts that the prices of e-books generally, including self-published e-books, decreased on average in the years following the introduction of the iBookstore, does not affect this conclusion. The Apple experts did not offer any scientifically sound analysis of the cause for this purported price decline or seek to control for the factors that may have led to it.

links in the chain of evidence that the Plaintiffs had to establish at trial.[62] They were:

> First is that the publishers sign Apple's agency agreements with an MFN and price caps.
>
> The second is that that MFN sharpened the publishers' incentives to demand agency from Amazon.
>
> The next is that that demand for agency convinces a company, Amazon, of the futility of continued resistance to agency.
>
> Amazon adopts agency in circumstances where absent the Apple MFN it would not have adopted agency.
>
> And the final chain in the alleged conspiracy is that the publishers raise prices to the price caps by agreement.
>
> All of these links in the chain are required for the government to meet its burden of proving that Apple participated in a price fixing scheme.

Apple also highlighted in its opening how much Apple likes low prices and that it did not know how the Publishers would price their e-books under the agency model.

Over the course of the trial, Apple abandoned each of these arguments. All of the "links" that Apple identified in its opening statement were established at trial,

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[62] In its pretrial memorandum of law, Apple's defense focused almost exclusively on *Monsanto*'s "tends to exclude" standard and its contention that Plaintiffs' evidence is insufficient to exclude the possibility of independent action. This remains Apple's chief argument in its defense.

and Apple did not argue otherwise in its summation. Apple similarly abandoned by summation its theory that Apple was unaware that the Publisher Defendants would use their new pricing authority to raise e-book prices; over the course of the trial, Apple's witnesses admitted that they expected the Publisher Defendants to raise their e-book prices to Apple's price caps. Instead, in the end, Apple appears to make six principal arguments in its defense.

First, it relies on the Supreme Court's decision in *Monsanto*, 465 U.S. 752, to assert that Apple is entitled to a verdict in its favor since the evidence does not "tend to exclude" the possibility that Apple acted in a manner consistent with its lawful business interests. Second, Apple argues that it never intended to conspire with the Publisher Defendants to raise e-book prices. Third, Apple argues that the Plaintiffs have failed to show that the Publisher Defendants actually "increased" e-book prices since, in the absence of Amazon's adoption of an agency model, the Publisher Defendants would have simply withheld e-books from Amazon. Apple also offers its own reading of different portions of the trial record, and that reading will be addressed as its fourth set of contentions. Fifth, Apple presents additional legal arguments suggesting that its conduct must be analyzed under the rule of reason. Finally, Apple argues that a verdict in favor of the Plaintiffs will set a dangerous precedent and will discourage businesses from entering other markets. Each of these defenses will be discussed in turn.

A. The *Monsanto* Decision and Apple's Independent Business Interests

Throughout these proceedings, Apple has relied on *Monsanto* and its "tends to exclude" formulation as the crown jewel of its defense. According to Apple, any fact-finder in this case must begin by answering the following question: "Does the evidence show that Apple acted to facilitate a conspiracy among the Publisher Defendants to force Amazon onto agency and raise prices, or rather was its conduct just as consistent with independent, unilateral action?" If the evidence regarding participation in a conspiracy is ambiguous, then Apple contends that, under *Monsanto*, the fact-finder may only find Apple liable if it concludes that Apple's participation in a conspiracy is "the more likely explanation" for its conduct. Apple also asserts that when the most natural inference from the evidence is that a defendant had a legitimate, independent reason for its actions, then no fact-finder may infer that it engaged in a conspiracy.

Applying this reading of precedent, Apple argues that it had legitimate, independent business reasons for executing the Agreements with the Publisher Defendants, and that these independent business reasons necessarily render any evidence of its participation in a conspiracy ambiguous. Because the Plaintiffs have been unable to show that Apple did not have legitimate reasons for acting as it did, Apple asserts that the Plaintiffs have failed to exclude the possibility that Apple acted lawfully. As a result, according to Apple, *Monsanto* dictates that a verdict be entered in its favor. Apple misreads *Monsanto* and its progeny. It also perceives ambiguity where none exists.

In *Monsanto*, 465 U.S. 752, the Supreme Court upheld a jury verdict that a manufacturer had engaged in a *per se* illegal vertical price-fixing scheme with "some of its distributors." The goal of the conspiracy was the termination of a rival distributor that was running a "discount operation." *Id.* at 756, 764-65. Because a manufacturer and its distributors "have legitimate reasons to exchange information about the prices and the reception of their products in the market," *id.* at 762, and because of dangers that flow from permitting an inference of conspiracy to be drawn "from highly ambiguous evidence," *id.* at 763, the Court held that a plaintiff must present evidence of "something more" than complaints from distributors to the manufacturer about their cost-cutting rival. *Id.* at 764. Using the phrase upon which Apple seizes, the Court observed that there "must be evidence that *tends to exclude* the possibility that the manufacturer and nonterminated distributors were acting independently." *Id.* (emphasis supplied). In other words, direct or circumstantial evidence must be present that "tends to prove that the manufacturer and others had a conscious commitment to a common scheme designed to achieve an unlawful objective." *Id.* (citation omitted).

Applying that standard, the Court examined the evidence presented at trial, and held that the direct and circumstantial evidence supported the jury's finding that there was an agreement between the manufacturer and one or more distributors to maintain prices. *Id.* at 767. In doing so, it noted that the choice between "two reasonable interpretations of the testimony" is properly left for the fact-finder. *Id.* at 768 n.12.

Two years later, in *Matsushita*, 475 U.S. 574, the Court returned to this topic in the context of summary judgment practice. It observed that "anti-trust law limits the range of permissible inferences from ambiguous evidence in a § 1 case." *Id.* at 588. The Court explained that "if the factual context renders respondents' claim implausible—if the claim is one that simply makes no economic sense—respondents must come forward with more persuasive evidence to support their claim than would otherwise be necessary. *Id.* at

587. Moreover, where there is conduct "as consistent with permissible competition as with illegal conspiracy," that conduct "standing alone" will not support an inference of conspiracy. *Id.* at 588. Thus, to "survive a motion for summary judgment or for a directed verdict, a plaintiff … must present evidence that tends to exclude the possibility that the alleged conspirators acted independently." *Id.* (citation omitted). Applying these principles to the case at hand, the Court noted that there could be no inference of a conspiracy when the accused "had no rational economic motive" to engage in a conspiracy and its conduct was "consistent with other, equally plausible explanations." *Id.* at 596. Therefore, to support liability, the evidence must "tend to exclude the possibility" that the accused engaged in legitimate behavior rather than engaging in "an economically senseless conspiracy." *Id.* at 597-98 (citation omitted).

These discussions of the "tend to exclude" formulations in *Monsanto* and *Matsushita* have occasioned commentary by academicians and courts of appeal. The Court of Appeals for the Second Circuit has warned that "[r]equiring a plaintiff to 'exclude' or 'dispel' the possibility of independent action places too heavy a burden on the plaintiff." *Publ'n Paper*, 690 F.3d at 63. According to the Second Circuit,

> [i]t is important not to be misled by *Matsushita*'s statement … that the plaintiff's evidence, if it is to prevail, must "tend … to exclude the possibility that the alleged conspirators acted independently." The Court surely did not mean that the plaintiff must disprove all nonconspiratorial explanations for the defendants' conduct. Not only did the court use the word "tend," but the context made clear that the Court was simply requiring sufficient evidence to allow a

> reasonable fact-finder to infer that the conspiratorial explanation is more likely than not.

Id. (citing Phillip E. Areeda and Herbert Hovenkamp, *Fundamentals of Antitrust Law*, § 14.03(b), at 14-25 (4th ed. 2011)). Accordingly, "if a plaintiff relies on ambiguous evidence to prove its claim, the existence of a conspiracy must be a reasonable inference that the jury could draw from that evidence; it need not be the *sole* inference." *Id.* Characterizing as a "trap" the fallacy that "if no single item of evidence presented by the plaintiff points unequivocally to conspiracy, the evidence as a whole cannot defeat summary judgment," the Court of Appeals for the Seventh Circuit has opined that the question for the fact-finder is simply "whether, when the evidence was considered as a whole, it was more likely that the defendants had conspired to fix prices than that they had not conspired to fix prices." *In re High Fructose Corn Syrup Antitrust Litigation*, 295 F.3d 651, 655-56 (7th Cir. 2002).

For the reasons described earlier in this Opinion, there is abundant direct and circumstantial evidence, and this Court has found, that Apple knowingly and intentionally participated in 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 the Publisher Defendants to raise the prices of e-books. *See Monsanto*, 465 U.S. at 764. Apple did not and could not have acted independently to achieve the results it achieved here. It required the coordinated effort and conscious commitment of the Publisher Defendants and Apple to change the business model for the distribution of e-books, impose that new model on Amazon against its will, and effect a significant increase in the retail prices of e-books. The finding that Apple engaged in an illegal conspiracy is based not simply on a finding that the "conspiratorial explanation is more likely than not," *Publ'n Paper*, 690 F.3d at 63; it is based on powerful direct evidence corroborated by compelling circumstantial evidence. Even if Apple had been successful at trial in showing that the evidence of its participation in the asserted conspiracy was equally balanced between two reasonable interpretations, *Monsanto*, 465 U.S. at 768 n.12, and it was not, the Plaintiffs have shown by a preponderance of the evidence that Apple violated the antitrust laws.

This conclusion is based on an evaluation of the entirety of the evidentiary record, including those portions on which Apple relies in arguing that it acted in ways that were consistent with its independent business interests. It is not surprising that Apple chose to further its own independent, economic interests. Such a motivation, however, does not insulate a defendant from liability for illegal conduct. It has long been observed that it is of "no consequence, for purposes of determining whether there has been a combination or conspiracy under s[ection] 1 of the Sherman Act, that each party acted in its own lawful interest." *United States v. General Motors Corp.*, 384 U.S. 127, 142 (1966).

To the extent that Apple is arguing that the evidence of its participation with the Publisher Defendants in the conspiracy is ambiguous, it is wrong. Instead, the evidence not only "tends to exclude the possibility" that Apple acted independently; it overwhelmingly demonstrates that it did not.

In asserting that its behavior was consistent with its legitimate business interests and with standard business practices, Apple emphasizes the following: it wanted to enter and compete successfully in the e-books market; it did not want to begin a business in which it would sustain losses; it wanted to avoid the windowing or withholding of e-books from its e-bookstore; the agency model, particularly one with price caps and an MFN, was a logical fit; and it was helpful to advise Publishers that it was offering the same terms to their competitors and would open the iBookstore only if it reached agreements with enough of them to have a successful e-bookstore. Apple contends that each of these practices was and is a lawful business practice. It argues that no proper inference that Apple conspired to raise price can be drawn from the several terms in the Agreements or the components of Apple's negotiating strategy because the Supreme Court has found actions of this type essential to the operation of efficient markets.

The Plaintiffs do not argue, and this Court has not found, that the agency model for distribution of content, or any one of the clauses included in the Agreements, or any of the identified negotiation tactics is inherently illegal. Indeed, entirely lawful contracts may include an MFN, price caps, or pricing tiers. Lawful distribution arrangements between suppliers and distributors certainly include agency arrangements. It is also not illegal for a company to adopt a form "click-through" contract, negotiate with all suppliers at the same time, or share certain information with them. Indeed, as Apple indicates, many common business practices have been found necessary for the efficient distribution of goods and services. *See Monsanto*, 465 U.S. at 763-64. That does not, however, make it lawful for a company to use those business practices to effect an unreasonable restraint of trade. And here, the evidence taken as a whole paints quite a different picture—a clear portrait of a conscious commitment to cross a line and engage in illegal behavior with the Publisher Defendants to eliminate retail price competition in order to raise retail prices.

Apple urges the Court to focus solely on each of the terms of the Agreements and to conclude that there is nothing inherently illegal in those terms or the contract as a whole. By asking the Court to focus exclusively on whether the final terms of the Agreements by themselves reflect an agreement in restraint of trade, Apple ignores the six weeks of negotiations leading up to their execution, when the conspiracy and Apple's participation in it took shape, and the weeks that followed, during which time the import of the Agreements became apparent. The Court is obligated to consider the totality of the evidence. Therefore, the Agreements must be considered in the context of the entire record. When that is done, it becomes evident that the caps for the price tiers were the fiercely negotiated new retail prices for e-books and that the MFN was the term that effectively forced the Publisher Defendants to eliminate retail price competition and place all of their e-tailers on the agency model.

Apple also argues that it is particularly unfair to find that it engaged in illegal conduct since Amazon and Google, among others, used similar negotiating tactics and included nearly identical terms, including MFNs, when they subsequently executed their own agency agreements with the Publishers. There are several reasons that this is not a persuasive argument.

First, it is no defense to participation in an illegal price fixing conspiracy to suggest that others did it too. Second, focusing on the precise terms of agency agreements and the extent to which they may have been similar is far too narrow a focus. The issue is not whether an entity executed an agency agreement or used an MFN, but whether it conspired to raise prices. Apple has pointed to no evidence that either Amazon or Google desired either to eliminate retail price competition or to raise retail prices. Quite the contrary. Amazon was adamant in its support of retail price competition and lower prices. It did not relinquish its control over retail pricing easily. As Penguin's Shanks described at trial, when Penguin demanded that Amazon yield its discretion over retail pricing, Amazon "yelled and screamed and threatened. It was a very unpleasant meeting." For its part, Google had been negotiating wholesale distribution agreements with Publishers and only switched to agency agreements at their insistence. Amazon was so hopeful that the Publisher Defendants would relent and revert to a wholesale model once they saw how much money they were losing with the agency model that it added a "model-parity" clause in its agreements.

In sum, Apple's independent business reasons for creating an e-bookstore and for adopting an agency model to do so have not created any ambiguity in the evidentiary record that should require hesitation before finding Apple liable. The totality of the evidence leads inextricably to the finding that Apple chose to join forces with the Publisher Defendants to raise e-book prices and equipped them with the means to do so.

B. Apple's Intent

Apple's second defense is related to its first. It argues that it never intended to conspire with the Publisher Defendants to raise the retail prices of e-books. Apple emphasizes that it was the Publisher Defendants who raised the prices, and Apple should not be found liable just because those Publishers used Apple's Agreements as a tool to force an industry change to the agency model and then used their newly acquired price-setting authority to raise the retail prices of e-books.

Apple asserts it was solely focused on accomplishing its core business objectives and on providing the best possible e-reading experience for consumers. Apple identifies those business objectives as the development of an iBookstore with comprehensive content and competitive pricing.[63] At trial, its witnesses stressed the benefits that accrued to readers from its iPad (color functionality, backlit screen, and video capability) and from the iBookstore e-reader software (landscape view option, an attractive page-curl function, and an end-to-end platform to browse, buy, and read an e-book in one seamless interface).

These business considerations undoubtedly drove Apple's conduct throughout its negotiations with the Publisher Defendants. Of course, Apple hoped to launch a new content store that was both profitable and popular. It described with enthusiasm at trial the improvements to the iBookstore that allowed cooks to learn the proper technique for preparing boeuf bourguignon by watching Julia Child, and allowed children to run their fingers over a color touchscreen while reading the illustrated pages of *Winnie the Pooh*. But, as the trial evidence made abundantly clear, there was more to Apple's entry into the trade e-book market than the presentation of innovative software on a remarkable device.

Apple's entirely appropriate or even admirable motives do not preclude a finding that Apple also intention-

[63] Apple uses the term "competitive" to convey that it wanted its prices to be the lowest in the marketplace, not to convey that it wanted prices arrived at through the process of competition.

ally engaged with the Publisher Defendants in a scheme to raise e-book prices. From its very first meetings with the Publishers, Apple appealed to their desire to raise prices and offered them a vision of how they could reach that objective. By the end of the trial, Apple's witnesses no longer denied that they fully understood that the Publisher Defendants would raise e-book prices to the Agreements' pricing caps as soon as the iBookstore appeared on the market. Understanding that no one Publisher could risk acting alone in an attempt to take pricing power away from Amazon, Apple created a mechanism and environment that enabled them to act together in a matter of weeks to eliminate all retail price competition for their e-books. 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. Apple's desire to create a profitable iBookstore on a superior e-reader does not obliterate the abundant record evidence that Apple made a commitment to act as the Publisher Defendants' partner in raising e-book prices materially above $9.99.

In a related argument, Apple contends that the Plaintiffs have paid unwarranted attention to the mechanism of an agency agreement and to the Agreements' MFN clause. Apple asserts that several reasons unrelated to price increases motivated its decision to endorse the agency model for distributing e-books along with an MFN clause, and that these business decisions thus cannot serve as evidence that Apple had any culpable intent to raise e-book prices. With respect to the agency model, Apple emphasizes that it was entering the e-book market at a time of turmoil, when Publishers were at war with their principal distributor. It points out that Barnes & Noble was actively considering the adoption of the agency model and that two of the Publishers—Hachette and HarperCollins—recommended the agency model to Apple at their December meetings.

But, the Plaintiffs have not argued that there is anything inherently wrong with an agency model or that Apple should not have advocated for its adoption. The question instead is whether competitors joined forces to eliminate price competition and raise prices and whether Apple knowingly and actively participated in that conspiracy. The Apple agency Agreements are important because they were the instrument that the conspirators chose to effect their scheme.

With respect to the MFN, Apple asserts that its sole intention in crafting that provision was to protect itself from price competition. It highlights the MFN's function in *lowering* consumer-facing prices, not raising them, and claims this fact undercuts any inference that the provision was intended as a mechanism to compel an industry-wide shift in price upward. But, just as Apple had multiple motivations in its negotiations, there was more than one function for the MFN. The MFN did lower the prices in the iBookstore below the price caps set in the tiers if a Publisher did not immediately move its other resellers to an agency arrangement. As described above, however, for that very same reason the MFN *also* forced the Publishers to convert all of their e-book distribution arrangements to agency arrangements and to raise e-book prices. Otherwise, a bad economic arrangement became a disastrous one for the Publishers. That is why Apple labeled the MFN an "elegant" alternative to its initial demand that the Publishers move all of their e-book retailers to an agency model.[64] Without that explicit requirement, Apple achieved the same end by means of the MFN.[65]

Finally, Apple argues that the contentious nature of the negotiations—particularly with respect to the caps on the price tiers—proves that there was no meeting of the minds to raise prices and therefore no conspiracy. But the fact that provisions, even key provisions, in the Agreements were the focus of hard-fought negotiations does not preclude a finding of liability. As the Seventh Circuit observed, "[a] co-conspirator who used his power to guide or direct other conspirators qualifies as an organizer even though his control was not absolute. The need to negotiate some details of the conspiracy with the cartel members also does not strip a defendant of the organizer role." *United States v. Andreas*, 216 F.3d 645, 679-80 (7th Cir. 2000).

It is true that the Publisher Defendants pushed for price caps, and thereby e-book prices, that were higher than those Apple thought consumers would "realistically" be willing to pay. But that was in the context of their overarching agreement to raise prices above the

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[64] Apple argued at trial that the MFN gave it more protection against price discrimination by Publishers than the requirement that the Publishers move all retailers to an agency arrangement. That is so as a theoretical matter, but there is no basis to find based on the trial record that Apple ever had reason to fear that the Publishers would use their power over retail pricing to lower prices anywhere. Instead, the evidence is that Apple feared retail price competition with Amazon. Apple preferred to compete with Amazon on the strength of its device rather than through price wars.

[65] Apple argued in summation, relying again on the *Monsanto* decision, that if the MFN had both illegal and legal purposes, then the existence of a lawful purpose would prevent a finding of liability. For the reasons described above, this argument misreads both the law and the record evidence.

$9.99 industry norm. It is also worth remembering that, when the Publisher Defendants pushed back during negotiations and asked for more and higher price caps, Apple agreed on January 16 to their demands. A meeting of the minds to raise e-book prices by working together could not be more clear on this record.

C. Windowing

A third defense that Apple introduced toward the end of the trial is that there was literally no "increase" in e-book prices and by definition therefore no conspiracy to raise e-book prices. It reasons that, but for its entry into the market, the Publisher Defendants would have withheld their books from Amazon. As a result, there would have been no established $9.99 price to raise. Apple argued in summation that, while its entry into the market meant that e-books were now available at $14.99 and $12.99, without their entry those e-books would not have been available at all.

This creative argument fails for several reasons. While it is difficult to know how the threats in late 2009 of four of the Publishers to withhold e-books from Amazon would have played out in 2010 if Apple had not entered the scene, there is no reason to find that windowing would have become widespread, long-lasting, or effective. Indeed, the Publishers (as well as Apple) realized that the delayed release of e-books was a foolish and even dangerous idea. The two largest Publishers—Random House and Penguin—never announced an intention to withhold e-books from Amazon. Those that did announce plans to window e-books only did so for 37 titles. At least one Publisher did internal research that showed that it would never make up sales lost due to the windowing of e-books. A Publisher had to assume that the lost sales were lost for good and that a competitor had gained a new reader in the process, unless the reader chose to purchase the e-book through the iBookstore or another e-tailer. The Publishers also recognized, and Apple concurred, that the delayed release of e-books encouraged piracy and posed an existential threat to the legitimate e-book industry.

Second, there was never any threat (before Apple encouraged one) to withhold all e-books. Many of the Publisher Defendants' most popular books were not, nor were they slated to be, windowed, including *True Compass*, the e-book Jobs bought for $14.99 at the Launch. Moreover, the Publisher Defendants raised the prices not just of New Releases but also of their backlist e-books.

Finally, it is ironic for Apple to claim credit for the end to windowing when it was Apple that encouraged the Publisher Defendants to present Amazon with a blanket threat of windowing for a seven month period, i.e., the defined term of a New Release in the Apple Agreements. As Amazon testified, it was that threat, delivered simultaneously by five of the Big Six, that left it with no alternative but to sign agency agreements with each of them. Viewed from any perspective, Apple's conduct led to higher consumer prices for e-books.

D. Characterization of the Evidence

Confronted with the substantial evidence of its participation in a conspiracy with the Publisher Defendants, Apple has offered a counter-narrative of the events that transpired in December 2009 and January 2010. To the extent that its version of key events has not already been addressed, it will be done so here and treated as Apple's fourth principal defense. Broadly speaking, Apple contends that the trial record shows that Apple acted independently and as a lawful participant in a series of negotiations that would be unexceptional for any new market entrant.

In making these assertions Apple must surmount several hurdles. First and foremost, the Plaintiffs' reading of the evidence is consistent with the documents. There is a voluminous documentary record in this case which repeatedly demonstrates Apple's willingness to join with the Publisher Defendants to eliminate retail price competition and raise the prices for e-books. The Opinion has quoted liberally from a fraction of these documents. The attempts by several witnesses to circumnavigate this documentary record were entirely unsuccessful and informed this Court's analysis of their credibility.[66]

Second, the circumstantial evidence provides ample corroboration for the Plaintiffs' theory of the case. There is very little dispute about the circumstantial evidence, and Apple has not been able to construct a persuasive alternative reading of this evidence.

Finally, Apple is confronted with the fact that the conspiracy succeeded. It not only succeeded, it did so

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[66] This Opinion has already described several instances in which testimony given by Cue and Sargent was unreliable. Other witnesses who were noteworthy for their lack of credibility included Moerer, Saul, and Reidy. Their demeanor changed dramatically depending on whether Apple or the Plaintiffs were questioning them; they were adamant in denials until confronted with documents or their prior deposition testimony; instead of answering questions in a straightforward manner, they would pick apart the question and answer it narrowly or avoid answering it altogether. Thus, the findings in this Opinion are informed by the documentary record, the circumstantial evidence, including an understanding of the competitive landscape in which these events were unfolding, and that portion of each witness' testimony that appeared reliable and credible.

in record-setting time and at the precise moment that Apple entered the e-book market.

Apple's narrative, by contrast, ignores much of the evidence or relies on strained readings thereof. To adopt Apple's theory, a fact-finder would be confronted with the herculean task of explaining away reams of documents and blinking at the obvious. A few remaining examples of Apple's contentions concerning the evidence follow.

1. *Initial Meetings with the Publishers*

Apple repeatedly argued at trial that its initial round of meetings with the Publishers in mid-December 2009 was merely an information-gathering exercise. It emphasizes that no binding commitments were entered into at these meetings and that a draft contract was not even circulated until weeks after the meetings. While Apple hoped to add an announcement of the iBookstore to the Launch of the iPad on January 27, as of these meetings it had no idea whether that would be possible.

Apple's entry into the conspiracy had to start somewhere, and the evidence is that it started at those initial meetings in New York City with the Publishers. Apple is a sophisticated company and had done its homework before its team flew to New York from California. It understood the depth of the Publishers' unhappiness with, and indeed fear of, the $9.99 price point and used that unhappiness and fear as its leverage. While the Apple team did listen in those meetings (and in doing so heard repeated expressions of anger at Amazon's pricing strategy), Apple also came prepared with a script. Using that script, across all its meetings, it set out several of its own conditions for entry into the market, but also offered the enticement that it knew would be music to the Publishers' ears: Apple was willing to sell its e-books at prices as high as $14.99. From that moment on, Apple had the Publishers' full attention.

The suggestion that Apple came to those New York meetings with no agenda is at odds with recitations of the meetings laid out in the contemporaneous documentary record. It is also at odds with common sense, and any appreciation of the daunting task that Apple had set for itself. Cue and his team are accomplished professionals. Apple had been studying the publishing industry for months. Newspapers were prominently featuring stories about the Publishers' battle with Amazon over pricing. Apple had less than two months to get commitments from the Publishers that it could announce at the Launch. Cue was personally invested in making that happen. The idea that Apple was simply a passive participant in the coordinated meetings that it had scheduled with the Publishers is not credible.

One could ask why Apple has taken pains to argue that the mid-December meetings were simply a commercial listening tour. It may matter to Apple because it is beyond dispute that Apple offered the Publishers a $14.99 price point at those meetings. Any finding that this was not a casual comment but a component of Apple's considered strategy confirms that Apple intended from the very beginning to assist the Publishers to shift the price of e-books upward.

2. *Conspiracy by Telepathy*

Apple asserts that there were too few meetings and telephone calls between Apple and any individual Publisher to establish its membership in the Publisher Defendants' conspiracy. Since there can be "no conspiracy by telepathy," Apple argues, there is insufficient evidence of a "meeting of the minds" to further any unlawful purpose between Apple and the Publisher Defendants.

Counting telephone calls during the key six-week period, particularly one that was interrupted by the Christmas and New Year holidays, is hardly a litmus test for knowing and intentional participation in a conspiracy. As Apple has observed, albeit in another context, it is the substance of the contacts, not their number, that counts.[67]

But, it is worth observing that in the short time between December 15 and January 26, Cue made three separate trips to New York City from Cupertino. His last trip was unprecedented in length—it lasted nine days—and as Cue described, for that entire period, if he was not eating or sleeping, he was negotiating. He also sent members of his team to New York to meet with the Publishers when he was not there, such as Moerer's trip to New York in the days following Apple's distribution of the Draft Agreement.

Cue and the Publishers also exchanged many telephone calls. Some of the more dramatic of these calls have already been highlighted. For example, Cue called three Publishers in late December to confirm that they would be willing to adopt an agency model across all of their resellers of e-books if that were a pathway to higher prices. He told Hachette's Thomas over the telephone that Apple was providing "the best chance for publishers to challenge the 9.99 price point." Cue called Reidy on January 21 to enlist her help in

[67] While admitting that very few e-books were actually withheld from Amazon by the four Publishers, Apple's Cue observed at trial that what mattered was which books were withheld, not how many.

convincing Macmillan's Sargent to execute the Agreement, and called Sargent to assist Macmillan's agency negotiations with Amazon.

And, of course, in this era, telephone calls are only one avenue of electronic communication. Cue and Moerer each exchanged numerous e-mails with the Publishers, many of which corroborate in writing Apple's commitment to the Publisher Defendants' scheme to raise e-book prices, including Cue's January 16 e-mail to the Publisher Defendants providing them with "significantly more tiers and higher prices" for e-books; Cue's message reminding Sargent of his commitment to move Amazon to agency and asserting that he "didn't believe we are asking you to do anything, you haven't told us you are doing" in following through with that promise; and Cue's blunt appeal to HarperCollins that the "basic deal" Apple is providing to the Publishers with its Agreement is "new release hardback pricing maximums which are way higher than $9.99 -> &12.99 or $14.99 for most."

In any event, while this conspiracy was complex to execute, its terms were relatively simple and required no extended discussion. The issue was whether Apple and the Publishers would join together to eliminate Amazon's power to set retail prices and then to raise prices to the point that Apple would permit. The most hotly contested negotiations revolved around just how high those prices would go. The risks and rewards of joining the conspiratorial enterprise were also easy to understand. The evidence is overwhelming that Apple and the Publisher Defendants' "minds met" and they moved as one to achieve their conspiratorial objective.

3. *Steve Jobs's Statements*

Compelling evidence of Apple's participation in the conspiracy came from the words uttered by Steve Jobs, Apple's founder, CEO, and visionary. Apple has struggled mightily to reinterpret Jobs's statements in a way that will eliminate their bite. Its efforts have proven fruitless.

Jobs's statements to James Murdoch that he understood the Publishers' concerns that "Amazon's $9.99 price for new releases is eroding the value perception of their products … and they do not want this practice to continue," and that Apple was thus "willing to try at the [$12.99 and $14.99] prices we've proposed," underscored Apple's commitment to a scheme with the Publisher Defendants to raise e-book prices. Jobs's purchase of an e-book for $14.99 at the Launch, and his explanation to a reporter that day that Amazon's $9.99 price for the same book would be irrelevant because soon all prices will "be the same" is further evidence that Apple understood and intended that Amazon's ability to set retail prices would soon be eliminated. When Jobs told his biographer the next day that, in light of the MFN, the Publisher Defendants "went to Amazon and said, 'You're going to sign an agency contract or we're not going to give you the books,'" Jobs was referring to the fact that Sargent was in Seattle that very day to deliver Macmillan's ultimatum to Amazon.

Apple could find no effective way at trial to escape the import of Jobs's remarks. While Apple stressed particular aspects of these statements, when taken as a whole and in context the statements remain powerful evidence of conspiratorial knowledge and intent. For example, Apple pointed to one line in Jobs's e-mail to James Murdoch where he muses about Amazon's $9.99 price point, "who knows, maybe they are right." But, focusing on that one line ignores paragraphs of statements, over two days of e-mails, in which Jobs tried to persuade Murdoch, and through him HarperCollins, to join with Apple in an effort to get control of and raise e-book prices. The sentence also does nothing to controvert Jobs's intent to raise e-book prices; it simply indicates his doubts over consumers' reaction to these higher prices. Jobs sums up his argument to Murdoch by urging him to "[t]hrow in with apple and see if we can all make a go of this to create a real mainstream ebooks market at $12.99 and $14.99." In this and every other instance, Apple's efforts to explain away Jobs's remarks have been futile.

4. *The Publishers Raised Prices, Not Apple*

Apple argues that, even if the Agreements "sharpened" the Publishers' incentives to force Amazon to distribute their e-books as an agent, at the end of the day it was the Publishers who had to decide whether to convert to an agency distribution system and it was the Publishers who had to decide whether to raise e-book prices once they were in charge of retail pricing. As Jobs maintained in response to consumer complaints, and as Cue asserted from the witness stand, Apple did not raise prices; the Publishers raised prices. Apple claims it should not be held liable for the "business decisions" the Publisher Defendants made in the early part of 2010.

Apple is correct that the conspiracy required the full participation of the Publisher Defendants if it were to achieve its goals. It is also correct that the Publishers wanted to change Amazon's pricing policies and to raise e-book prices, and that they had wanted to do that for many months before Apple arrived on the scene. But, those facts do not erase Apple's own intentions in entering into this scheme. Apple did not want to compete with Amazon on price and proposed to the Publishers a method through which both Apple and the

Publishers could each achieve their goals.[68] Apple was an essential member of the charged conspiracy and was fully complicit in the scheme to raise e-book prices even though the Publisher Defendants also had their own roles to play.

Apple also attempts to argue in this regard that it cannot be held responsible for the Publisher Defendants' actions because it never knew the Publishers were working together to raise prices. To the contrary, the evidence consistently points not only to Apple's awareness but also its facilitation of the Publisher Defendants' collective action. From the beginning, Apple conducted its campaign with the understanding that it wanted all six, and needed at least four, of the Publishers to join its terms. Cue urged the Publisher Defendants' CEOs to have discussions with one another to clarify aspects of the Agreements or to convince others to sign on. This enterprise depended on joint action. As Apple fully appreciated, the Publishers required the protection offered by collective action if they were to succeed in taking control over prices from Amazon and changing the public's perception about how much books should cost.

E. *Per Se* Liability

Apple strenuously objects to the Plaintiffs' contention that this case may be analyzed as a *per se* violation of the Sherman Act. It asserts that there are two reasons why this Court may only apply a rule of reason analysis. The first hinges on the fact that Apple is a

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[68] The record is equivocal on whether Apple itself desired higher e-book prices than those offered at Amazon. It is unequivocal though that Apple embraced higher prices so convincingly that the Publishers believed that Apple was content with, and even wanted, higher prices, and that Apple's cooperation with the Publisher Defendants enabled them to raise prices.

vertical player vis-à-vis the Publisher Defendants, and that courts apply the rule of reason in assessing the legality of agreements between vertical players in an industry. Second, it contends that Plaintiffs' reliance on the traditional "hub and spoke" conspiracy cases which found *per se* violations of the antitrust laws, such as *Toys "R" Us*, 221 F.3d 928, and *Interstate Circuit,* 306 U.S. 208, is not appropriate here because Apple was a new market entrant and not a dominant player. Both of these arguments fail.

While vertical restraints are subject to review under the rule of reason, *Leegin*, 551 U.S. at 907, Apple directly participated in a horizontal price-fixing conspiracy. As a result, its conduct is *per se* unlawful. The agreement between Apple and the Publisher Defendants is, "at root, a horizontal price restraint" subject to *per se* analysis. *In re: Elec. Books Antitrust Litig.*, 859 F. Supp. 2d 671, 685 (S.D.N.Y. 2012). As such, it is not properly viewed as either a vertical price restraint or solely through the lens of traditional "hub and spoke" conspiracies.

In any event, the fact that Apple was not a dominant player in the relevant market in no way diminishes the instructive value of the traditional hub and spoke conspiracy cases here. Courts have never found that the vertical actor *must* be a dominant purchaser or supplier in order to be considered a traditional "hub," only that this is "generally" the case. *See Howard Hess Dental Labs. Inc. v. Dentsply Int'l, Inc.*, 602 F.3d 237, 255 (3d Cir. 2010). Moreover, as Apple has conceded in its filings, the "hub" defendant's liability in those cases existed because "there was no doubt … that the 'hub' defendant was aware of the purported scheme—the only question was whether the horizontal defendants agreed to it." *See Interstate Circuit*, 306 U.S. at 222 (defendant organized and implemented the plan); *Toys "R" Us*, 221 F.3d at 933 (defendant communicated messages from manufacturer to manufacturer and "served as the central clearinghouse for complaints about breaches in the agreement"). Here we have every necessary component: with Apple's active encouragement and assistance, the Publisher Defendants agreed to work together to eliminate retail price competition and raise e-book prices, and again with Apple's knowing and active participation, they brought their scheme to fruition.

The observations of the Supreme Court in *Interstate Circuit* are equally apt here:

> [i]t was enough that, knowing that concerted action was contemplated and invited, the distributors gave their adherence to the scheme and participated in it. Each distributor was advised that the others were asked to participate; each knew that cooperation was essential to successful operation of the plan. They knew that the plan, if carried out, would result in a restraint of commerce, which … was unreasonable within the meaning of the Sherman Act, and knowing it, all participated in the plan.

306 U.S. at 226-27.

F. Avoiding a Dangerous Precedent

Finally, Apple warns that a ruling against Apple would set a dangerous precedent. It predicts that a finding that it violated the antitrust laws will deter entry into concentrated markets and punish innovation. It contends that its conduct was pro-competitive and created a healthier market. Censuring Apple for entering a tumultuous new market, in Apple's view, will have a "chilling and confounding … effect not only on commerce but specifically on content markets throughout this country."

It is certainly true that our nation's antitrust laws should be applied with care. Courts must be sensitive to the unique features of any market and the ambiguities of commercial conduct to avoid chilling lawful competition. Providing new entrants with the ability to access markets has long been a mainstay of our economy and any court should be wary of discouraging such access or interfering with the natural evolution of markets. *See, e.g.*, *United States v. Grinnell Corp.*, 384 U.S. 563, 589 (1966). As the Second Circuit observed in *Capital Imaging*, 996 F.2d 537, "[a]ntitrust law is not intended to be as available as an over-the-counter cold remedy, because were its heavy power brought into play too readily it would not safeguard competition, but destroy it." *Id.* at 539.

It is not entirely clear to what Apple is alluding, however, when it describes its pro-competitive behavior and creation of healthy competition. If it is alluding to the Launch of the iPad, a revolutionary device that has encouraged innovation and competition, then its conduct can fairly be described as pro-competitive. But, this case has been only incidentally about the iPad. The iBookstore was not an essential feature of the iPad, and the iPad Launch would have occurred without any iBookstore. It was the pre-existing, remarkable features of the iPad that made the iBookstore an obvious addition to the device.

If Apple is alluding to the fact that Amazon's Kindle bookstore was the dominant e-retailer for books in 2009, and that the arrival of the iBookstore created another e-retailer, that is true. But, as this Opinion explains, 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 of the iBookstore brought less price competition and higher prices.[69]

If Apple is suggesting that Amazon was engaging in illegal, monopolistic practices, and that Apple's combination with the Publisher Defendants to deprive a monopolist of some of its market power is pro-competitive and healthy for our economy, it is wrong. 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. If it was, however, the remedy for illegal conduct is a complaint lodged with the proper law enforcement offices or a civil suit or both. Another company's alleged violation of antitrust laws is not an excuse for engaging in your own violations of law. Nor is suspicion that that may be occurring a defense to the claims litigated at this trial.

If Apple is suggesting that an adverse ruling necessarily implies that agency agreements, pricing tiers with caps, MFN clauses, or simultaneous negotiations with suppliers are improper, it is wrong. As explained above, the Plaintiffs have not argued and this Court has not found that any of these or other such components of Apple's entry into the market were wrongful, either alone or in combination. What was wrongful was the

[69] As for some of the notable features of the iBookstore itself, features such as a page curl, Apple was not the first to invent these concepts. Nonetheless, having the creativity and commitment of Apple invested in the enhancement of a product like the iBookstore is extremely beneficial to consumers and competition.

use of those components to facilitate a conspiracy with the Publisher Defendants.

It is doubtful that Apple is suggesting that the only way it could have entered the e-book market was to agree with the Publisher Defendants to raise e-book prices. Apple, often through expert negotiations conducted by Cue, has entered many new content markets. It did not attempt to argue or show at trial that the price of admission to new markets must be or is participation in illegal price-fixing schemes.

While a Court must take seriously a prediction that its decision will harm our nation's economy, particularly when made by skilled counsel on behalf of an esteemed company, it is difficult to see how competition will be stifled by the ruling in this Opinion. This Opinion's findings arise from the specific events that unfolded in the trade e-book market as 2009 became 2010. It does not seek to paint with a broader brush.

In the end, it is essential to remember that the antitrust laws were enacted for "the protection of *competition*, not *competitors*." *Brown Shoe Co. v. United States*, 370 U.S. 294, 320 (1962). The question in this case has always been a narrow one: whether Apple participated in a price-fixing scheme in violation of this country's antitrust laws. Apple is liable here for facilitating and encouraging the Publisher Defendants' collective, illegal restraint of trade. Through their conspiracy they forced Amazon (and other resellers) to relinquish retail pricing authority and then they raised retail e-book prices. Those higher prices were not the result of regular market forces but of a scheme in which Apple was a full participant.

CONCLUSION

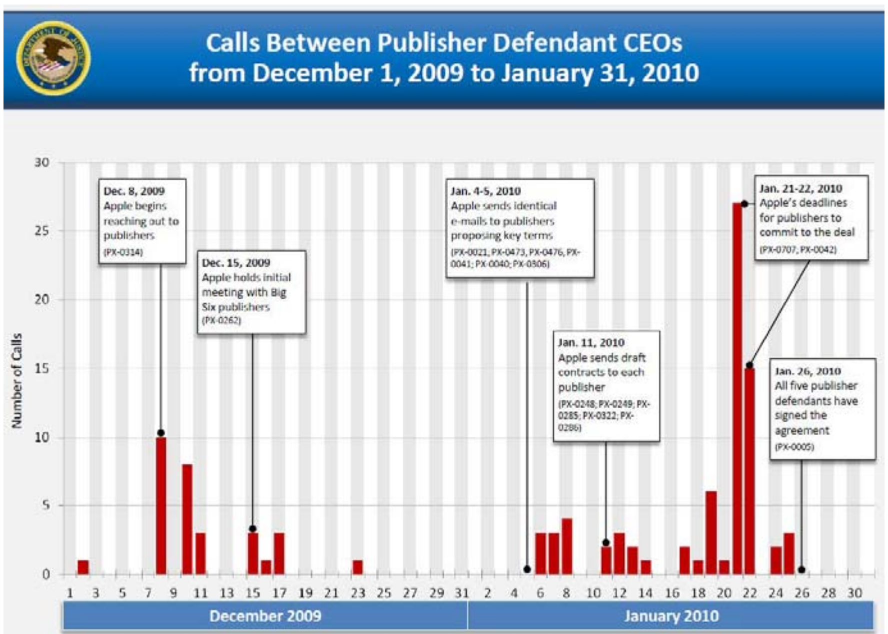
Based on the trial record, and for the reasons stated herein, this Court finds by a preponderance of the evidence that Apple conspired to restrain trade in violation of Section 1 of the Sherman Act and relevant state statutes to the extent those laws are congruent with Section 1. A scheduling order will follow regarding the Plaintiffs' request for injunctive relief and damages.

SO ORDERED:

Dated: New York, New York
July 10, 2013

/s/ Denise Cote
DENISE COTE
United States District Judge

Appendix A



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