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Antitrust standing and the new economy

Innovation and network effects have the potential to alter the traditional analysis

BY PETER T. BARBUR
AND JONATHAN J. CLARKE

The antitrust standing doctrine, which is now more than three decades old, faces new challenges brought on by a shift in our understanding of competition. With the growth of the Internet, mobile telephony and other research and development-intensive industries characterized by rapid product cycles, antitrust has embraced a more sophisticated model of competition. Although courts have begun to apply this new perspective to substantive antitrust doctrine, they are only beginning to grapple with these issues in the antitrust standing context. Two aspects—network effects and innovation—of what is often termed the "new economy" have the potential to alter antitrust standing analysis.

Section 4 of the Clayton Act provides that "any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefore…and shall recover threefold the damages by him sustained." Courts initially interpreted this provision to provide a private right of action to anyone who was injured as a proximate result of an antitrust violation. Some practitioners viewed this broad interpretation as overburdening the federal courts with antitrust claims and permitting plaintiffs to recover damages for harms unrelated to the purposes of the antitrust laws.

The U.S. Supreme Court ended that trend with its 1977 opinion in *Brunswick Corp. v. Pueblo Bowl-O-Mat*, 429 U.S. 447 (1977). In *Brunswick*, the Court held that to recover damages under the antitrust laws, private plaintiffs must prove more than that their injury was caused by anti-competitive conduct. Instead, "[p]laintiffs must prove antitrust injury, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful." Although its importance was not immediately clear—*Continental T.V. Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977), and *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), which were decided during the same term as *Brunswick*, received more attention at the time—*Brunswick* has become recognized as a pivotal case in antitrust law.

Antitrust standing doctrine has continued to develop and today is fairly complex. At its most basic level, though, courts apply a two-part test to determine whether a plaintiff has antitrust standing. First, they consider whether the plaintiff has suffered an antitrust injury as described in *Brunswick*. Second, they evaluate several factors to determine whether the plaintiff is the proper one to enforce a given claim: the directness or indirectness of the asserted injury; the existence of an identifiable class of persons whose self-interest would normally motivate them to vindicate the public interest in antitrust enforcement; the speculativeness of the alleged injury; and the difficulty of identifying damages and apportioning them among direct and indirect victims so as to avoid duplicative recoveries.

NETWORK EFFECTS

A network effect exists when an increase in the number of users of a product or service increases the value of that good or service to others. Network effects are common in several technology-driven markets and are often credited by courts with raising entry barriers and creating market power.

In *U.S. v. Microsoft Corp.*, 253 F.3d 34, 55 (D.C. Cir. 2001) (en banc), for example, the U.S. Court of Appeals for the D.C. Circuit found that Microsoft largely owed its dominance in the personal computer operating market to the existence of a network effect common to software markets: "(1) most consumers prefer operating systems for which a large number of applications have already been written; and (2) most developers prefer to write for operating systems that already have a substantial consumer base."

More specifically, application software is typically written to connect or call on applications programming interfaces (APIs). These APIs permit the application to use the services of the underlying software platform (e.g., Microsoft's Windows operating system).

For example, rather than having to rewrite code for drawing a box on a computer screen, an application can access the operating system API that performs that function.

Because Microsoft had the most users, application developers were most likely to write software that would dock with Windows, which in turn made Windows the most desirable operating system for users. Internet browsers and middleware technologies threatened to undermine that dominance by making their own APIs available to application makers. If enough software developers were to write applications using browsers or middleware rather than the underlying operating system as a platform, which operating system a device ran on would become less relevant. See, generally, Franklin M. Fisher, "Innovation and Monopoly Leveraging," Dynamic Competition and Public Policy: Technology, Innovation, and Antitrust Issues (J. Ellig ed., Cambridge Univ. Press 2000).

While it is commonly understood that the existence of network effects should figure prominently in the analysis of entry barriers in many technology-driven markets, this same dynamic may also play a role in antitrust standing analysis. In *Novell v. Microsoft Corp.*, 505 F.3d 302 (4th Cir. 2007), the 4th Circuit affirmed a district court opinion holding that the maker of WordPerfect had antitrust standing to assert claims based on allegations that Microsoft, believing that WordPerfect constituted a middleware threat to its operating system monopoly, damaged the product by withholding interoperability information, coercing original equipment manufacturers into not licensing it, and requiring Novell to use Windows-specific technologies that degraded the performance of the product on other operating systems.

Although Novell was not a competitor or consumer in the personal computer operating system market, the court found that Microsoft's anti-competitive conduct had potentially injured Novell by encouraging a network effect that would disadvantage Novell: "Microsoft's use of its monopoly power in the operating-system market to foreclose the distribution channels for Novell's applications…would have naturally tended to decrease Novell's market share and consequently decrease the value of its applications.…This loss of market share could make a competing operating system featuring Novell's office-productivity applications less attractive to consumers, harming that competing operating system's potential to surmount the barrier protecting the Windows monopoly." Id. at 316.

The 4th Circuit reached a different result in *Kloth v. Microsoft Corp.*, 444 F.3d 312 (4th Cir. 2006), finding that individual purchasers of applications and operating system software products lacked standing to assert claims against Microsoft for essentially the same conduct.

Network effects are common in several technology-driven markets.

INNOVATION AND ANTITRUST STANDING

Courts often consider whether substantive antitrust law, as applied, will promote or hinder innovation. Although courts also sporadically consider whether harm to innovation might constitute an antitrust injury entitling a plaintiff to standing, a decrease in innovation has not proved to be a promising basis for finding an antitrust injury.

Generally speaking, alleging that anti-competitive conduct has resulted in harm to innovation has not permitted plaintiffs to overcome established barriers to demonstrating antitrust standing. In two related cases, for example, purchasers of cellphones brought antitrust suits against Qualcomm Inc. alleging that it had engaged in anti-competitive licensing of its patented chipset technology. *Lorenzo v. Qualcomm Inc.*, 603 F. Supp. 2d 1291 (S.D. Calif. 2009); *Meyer v. Qualcomm*, No. 08 Civ. 655, 2009 WL 539902 (S.D. Calif. March 3, 2009). The plaintiffs asserted that the licensing practices harmed chipset manufacturers in the form of supracompetitive prices and the impairment of nonprice competition in innovation, and that these harms were passed down through chipset manufacturers, device manufactures and vendors to end users such as the plaintiffs.

Applying traditional standing principles, the court held that the plaintiffs' injury was too remote from Qualcomm's alleged antitrust violations to support antitrust standing because the plaintiffs attempted to trace these harms through three levels of a supply chain that was affected by a multitude of factors. The plaintiffs' allegation that the anti-competitive conduct harmed innovation did not alter the way in which the court analyzed a traditional standing concept like remoteness.

Nevertheless, some courts have been receptive to arguments that antitrust standing can be grounded in the idea that anti-competitive conduct has prevented new and potentially innovative products from coming to market. In *Aventis Environmental Science USA L.P. v. Scotts Co.*, 383 F. Supp. 2d 488 (S.D.N.Y. 2005), for example, plaintiff Aventis alleged that defendants Scotts Co. and Monsanto Co. had entered into an agreement designed to exclude Aventis' Finale product from the market for nonselective residential herbicides, a market dominated by Monsanto's RoundUp product. Among other things, the defendants argued that there was no evidence of an antitrust harm to competition.

The district court disagreed, finding that the plaintiff's expert testimony had provided evidence showing that the defendants' agreement to exclude Finale had led to an allegedly improved version of RoundUp developed by Monsanto not being introduced to market. According to the court, "[e]vidence of such a retardation of innovation and subsequent decrease in the quality of [nonselective herbicides] potentially available to consumers, if believed, could qualify as a harm to competition and consumers." Id. at 504.

Innovation and network effects are commonly cited as major factors in the "new economy" and have played a prominent role in substantive antitrust analysis over the past decade. While, as described, they are also beginning to raise issues for antitrust counsel in the standing context, this movement remains inchoate and faces many challenges.

Peter T. Barbur is a partner, and Jonathan J. Clarke is an attorney, in the litigation department of Cravath, Swaine & Moore in New York.