

# KIRKLAND ALERT

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## Supreme Court Decision Expected Soon in Amex “Anti-Steering” Case

On February 26, 2018, the U.S. Supreme Court heard oral argument in the matter of *Ohio v. American Express*. The issue before the Court was how the “rule of reason” should be applied in a two-sided market like the credit card industry, where companies like American Express simultaneously serve both merchants and cardholders during the course of a transaction.

### *Procedural Posture*

In 2010, the U.S. and several states sued American Express (Amex), Visa and MasterCard, claiming that the so-called “anti-steering” provisions of their respective merchant agreements unreasonably restrained trade in violation of Section 1 of the Sherman Act. The anti-steering provisions at issue prevent merchants from “steering” a customer who presents, for example, an Amex card to another type of credit card, like a lower-cost Visa or MasterCard. Visa and MasterCard settled with the government before trial and removed their anti-steering provisions, and Amex proceeded to trial on its own.

After a seven-week bench trial in 2014 in the Eastern District of New York, Judge Nicholas Garaufis ruled that the government had satisfied its burden of proving a Section 1 violation because it had shown harm to competition in the merchant network services market. In its analysis, the court applied the rule of reason — because the anti-steering provisions are vertical non-price restraints — and not the *per se* standard, which is typically reserved for horizontal price restraints, like price-fixing, where the anticompetitive effects are presumed. Under step one of the rule of reason, the court found that the government had adequately proven anticompetitive harm in the relevant market. Under step two, Amex failed to show that the procompetitive effects outweighed that harm.

Amex appealed, and a unanimous Second Circuit panel reversed, holding that the district court erred in its application of the rule of reason, including by improperly defining the market to include only the merchant side. Instead, the Second Circuit found that the proper market definition included both sides of the market, cardholder and merchant services. Because the government failed to prove a *net* anticompetitive effect of the anti-steering rules on the overall market in step one, it had failed as a matter of law to prove harm. The government sought and the Second Circuit denied rehearing and rehearing *en banc*.

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### *Supreme Court Appeal and Argument*

The states petitioned the Supreme Court for *certiorari*, arguing that the government had adequately made a *prima facie* showing of harm in the merchant market under step one of the rule of reason, and that any evidence relating to the consumer side of the market was Amex's burden under the step-two showing of procompetitive effects. Although the U.S. did not join the states in their petition for *certiorari*, it did ultimately file an *amicus* brief in support of the states, while at the same time asking the Supreme Court *not* to hear the case. Once *certiorari* was granted, the U.S. requested time and was heard at argument.

Ohio's Solicitor General, Eric Murphy, argued first and for the states. Mr. Murphy spoke for only a few minutes before he was interrupted by Justice Neil Gorsuch, who signaled that he was primarily concerned with protecting consumers, and not merchants. Justice Gorsuch also questioned Mr. Murphy on the government's failure to prove at trial that, on a net basis, consumers paid more as a result of the anti-steering rules. Justice Anthony Kennedy pointed to an *amicus* brief filed by antitrust and economics scholars, who argued that the court should focus its analysis on the overall increase in output, an indicator that competition had not been harmed by the anti-steering rules.

In what was decidedly a hot bench, Justice Ruth Bader Ginsberg also questioned Mr. Murphy, asking him to "comment on the Second Circuit's view that what's involved is a credit card transaction, and that includes both services to merchants and services to cardholders and that you can't just deal with one and ignore the other." Mr. Murphy respectfully disagreed with the Second Circuit's view and instead argued that merchant and cardholder services were separate product markets.

The U.S. Deputy Solicitor General, Malcom Stewart, argued for the U.S. and echoed Mr. Murphy's argument that there were two distinct product markets at issue, and that the Second Circuit erred when it "collapsed" them into one market. Justice Gorsuch again led the questioning, asking Mr. Stewart about the complex nature of vertical restraints and the hazards of judicial intervention where competitive effects are hard to determine. Mr. Stewart admitted that was one of the very reasons the U.S. had decided not to petition for *certiorari* in the matter. Even now that it was under review, Mr. Stewart argued that any decision in favor of the states could be narrowly tailored so as to avoid Justice Gorsuch's concerns.

Both Justice Elena Kagan and Justice Kennedy questioned Mr. Stewart about the government's position that the effect on cardholders should not be evaluated under step one of the rule of reason, with Justice Kennedy commenting that such a one-sided analysis would be "dangerous".

Evan Chesler of Cravath, Swaine and Moore LLP argued for Amex, and was questioned intensely by Justice Sonia Sotomayor about consumer choice and the nature of competition at the point of sale. Justice Sotomayor's overarching point was that

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the anti-steering rules prevented merchants from offering a discount to customers for using a lower-cost credit card. That lack of competition at the point of sale with respect to price concerned the Justice. Mr. Chesler argued in response that any price charged by Amex to merchants needed to be offset by the consumer rewards being paid to customers in order to calculate the net price.

Justice Stephen Breyer also questioned Mr. Chesler, signaling that he was not overly concerned with reviewing the merchant side of the market alone in step one, so long as the consumer side of the market was evaluated in step two. Justice Breyer also expressed concern with the anticompetitive impact of merchants being unable to tell consumers that Amex may charge merchants more for transactions than Visa and MasterCard.

### *Conclusion*

Regardless of the outcome, practitioners and scholars alike see this case as an important opportunity for the Supreme Court to provide additional guidance on the appropriate application of the rule of reason, as well as the effect of two-sided markets on that analysis.

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If you have any questions about the matters addressed in this *Kirkland Alert*, please contact the following Kirkland author or your regular Kirkland contact.

Katherine A. Rocco  
Kirkland & Ellis LLP  
601 Lexington Avenue  
New York, NY 10022  
[www.kirkland.com/krocco](http://www.kirkland.com/krocco)  
+1 212 446 4790

### **Disclosure**

Prior to joining Kirkland, Katherine Rocco practiced at Cravath, Swaine & Moore LLP, where she represented American Express, including in the matter discussed here.

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