

# American Express and two-sided antitrust Markets: Coming to a network near you

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On 25 June the U.S. Supreme Court [ruled](#) in *Ohio v. American Express* that American Express (Amex) did not violate the federal antitrust laws by directing merchants not to “steer” cardholders to alternative credit cards as a condition for accepting American Express cards. In a groundbreaking decision, the Court held that analyzing the effect of the anti-steering rules on merchants alone was inappropriate, and that, instead, the combined effect of the rules on *both* merchants and cardholders should be analyzed in a two-sided “transaction platform” market. The decision likely will have broader implications far beyond the credit card industry on how to define (and evaluate effects) in markets where platforms or intermediaries connect groups of buyers and sellers.

## Background

One way in which Amex differs from other credit card companies is that Amex charges merchants a higher fee in order to provide greater rewards and other benefits to cardholders. Merchants want access to Amex cardholders because they tend to be wealthier and spend more, but merchants also would prefer to process the transaction with a lower fee, so they steer buyers to other cards at the point of sale. To address these incentives, Amex created the anti-steering rules to prohibit merchants from steering Amex cardholders to lower cost cards at the point of sale.

In 2010, the U.S. Department of Justice (DOJ), joined by attorneys general of 18 states [sued](#) Amex alleging that Amex’s use of anti-steering rules violated Section 1 of the Sherman Act. The government argued that these provisions reduced competition among credit card companies that would otherwise have resulted in a reduction in the merchant fees that those companies charge to process transactions. American Express countered that the government failed to properly account for the effect of the anti-steering rules on cardholders, who benefit from increased cardholder rewards and other benefits. The dispute therefore centered on whether the government’s evidence of increased merchant fees alone was sufficient to show harm to competition. In 2015, the district court [ruled](#) in favor of the government. A year later, the Second Circuit [reversed](#), finding that the district court’s analysis did not properly account for the effect of the rules on cardholders. Eleven states, led by Ohio, subsequently [petitioned](#) the Supreme Court to grant certiorari. Once the Supreme Court granted certiorari, the DOJ joined the states’ efforts in opposing Amex’s anti-steering provisions.

## The Opinion

In a 5 to 4 decision authored by Justice Thomas, the Supreme Court [affirmed](#) the Second Circuit. The majority began by characterizing credit card services as a two-sided “transaction platform” market in which a company “offers different products or services to two different groups who both depend on the platform to intermediate between them” and in which the company “cannot make a sale to one side of

the platform without simultaneously making a sale to the other” side of the platform. The majority explained that such markets are characterized by “indirect network effects,” meaning that “the value of the services that the two-sided platform provides increases as the number of participants on both sides of the platform increases.” With respect to the credit card market, for example, the method of payment becomes “more valuable to cardholders when more merchants accept it” and “more valuable to merchants when more cardholders use it.”

The Court went on to explain why it is important to properly identify “transaction platform” markets. Noting that, “[s]ometimes indirect network effects require two-sided platforms to charge one side much more than the other,” the Court said that “[t]he optimal price might require charging the side with more elastic demand a below-cost (or even negative) price.” In other words, the Court held that a company may lawfully “subsidize” customers on side A with elastic demand by charging higher prices to customers on side B with inelastic demand.

The core of the Court’s holding is that competitive effects on both cardholders and merchants must be evaluated together in a single relevant market: “the fact that two-sided platforms charge one side a price that is below or above cost reflects differences in the two sides’ demand elasticity, not market power or anticompetitive pricing. Price increases on one side of the platform likewise do not suggest anticompetitive effects without some evidence that they have increased the overall cost of the platform’s services. Thus, courts must include both sides of the platform—merchants and cardholders—when defining the credit card market.” The Court held that “competition cannot be accurately assessed by looking at only one side of the platform in isolation.”

As the Court explained, “[e]vidence of a price increase on one side of a two-sided transaction platform cannot by itself demonstrate an anticompetitive exercise of market power.” Because the market had to be defined to include both merchants and cardholders, the government’s reliance on higher merchant fees alone “misses the mark because the product that credit card companies sell is transactions, not services to merchants.” Instead, to prevail, the government would have had to “demonstrate anticompetitive effects on the two-sided credit card market as a whole” by proving that Amex’s anti-steering provisions “increased the cost of credit card transactions above a competitive level, reduced the number of credit card transactions, or otherwise stifled competition in the credit card market.”

The government had presented evidence that some percentage of Amex’s merchant fee increases were not spent on cardholder rewards or other benefits. But the Court held that this evidence of an increase in the “net” price of transactions was insufficient standing alone because the government failed to provide evidence that such net prices were high relative to what would prevail in a competitive market. The Court also noted the lack of evidence of a reduction in output given that the number of credit card transactions overall grew by 30 percent between 2008 and 2013. And it acknowledged that Visa and MasterCard had constrained Amex’s ability to raise merchant fees and had achieved broader merchant acceptance by charging lower fees. Because the government had not carried its *prima facie* burden of proof under the rule of reason to prove harm to competition, it was unnecessary to consider procompetitive benefits.

## **Implications**

The *Amex* decision will have significant consequences in markets that could be characterized as two-sided transaction platforms. While the opinion provides some guidance, it leaves open many questions for lower courts to resolve, including:

**When is market definition necessary?** Plaintiffs often seek to rely on direct evidence of anticompetitive effects to demonstrate market power in lieu of formally defining a relevant market, based largely on language in [FTC v. Indiana Federation of Dentists](#). However, in a footnote, the Court read that opinion narrowly as applying only to horizontal restraints and strongly suggested that market definition is required in every case involving a vertical restraint. In other words, plaintiffs may not rely on evidence of alleged actual anticompetitive effects to avoid market definition in vertical cases. This portion of the Court’s ruling may have implications even beyond two-sided “transaction platform” markets.

**What markets are “transaction platform” markets?** The Court’s opinion does not identify the industries that might be considered “transaction platforms.” Instead, the Court focused on whether there are “indirect network effects,” noting that, even if a platform can be characterized as two-sided, it “should be treated as one-sided when the impacts of indirect network effects and relative pricing in that market are minor.” For example, even though newspapers connect readers and advertisers, the Court said that such markets should be considered “one sided” because the indirect network effects only work in one direction: while advertiser demand increases as the number of readers increases, readers are indifferent to the number of advertisers. While it remains unclear what markets might be considered two-sided “transaction platforms,” companies in particular industries that may satisfy the Court’s standard should carefully consider the implications of the Amex decision when analyzing antitrust issues. Potential examples include:

- **E-commerce:** User demand for online shopping increases as the number of consumer products featured on the operator’s website increases.
- **Healthcare:** Subscriber demand for health insurance increases as the number of providers in the insurer’s network increases.
- **Media:** Subscriber demand for a network increases as the amount of content on the network increases.
- **Ride-sharing:** User demand for a ride-sharing app increases as the number of drivers that participate on the app increases.
- **Travel:** User demand for online travel planning and comparative flight search services increases as the number of airlines selling tickets through the website increases.

**How will courts analyze effects in “transaction platform” markets?** The Court explained that evidence of price effects on one side of a two-sided market is not sufficient. Moreover, the Court held that it is not sufficient to show that price increases on one side of the market (e.g., merchant fee increases) were only partially passed through as price reductions on the other side of the market (e.g., cardholder rewards). Instead, the opinion suggests that a plaintiff must show that the challenged restriction resulted in a higher “net” price (or lower output) relative to what would prevail in a competitive market. The dissent (authored by Justice Breyer) voiced concerns with the burden this standard could impose on plaintiffs, noting that “to require actual proof of reduced output is often to require the impossible.” The Amex decision certainly previews complex competitive effects analyses, and it remains to be seen what evidence lower courts will accept in balancing the costs and benefits of network effects in two-sided “transaction platform” markets.

If you have questions about what the *Amex* decision may mean for your industry or your company please contact us for further guidance.

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