GCR NEWS

# Two sides of the Atlantic on two-sided markets

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Michael Weiner, Alec Burnside and Adam Kidane

*At the end of June, the US Supreme Court used the term "two-sided market" for the first time. Its* American Express *ruling promises to fuel many years of debate, including whether the US court has diverged from its European counterpart's 2014 judgment in* Cartes Bancaires*. Three Dechert lawyers – partner* ***Michael Weiner*** *in New York; and partner* ***Alec Burnside*** *and associate* ***Adam Kidane*** *in Brussels – take a transatlantic look at the question.*

In *Ohio v American Express*, the US Supreme Court held that the "anti-steering" provisions in American Express's merchant agreements – which require a retailer not to "steer" customers away from using their Amex cards, such as to a card charging a lower rate of commission – did not violate section 1 of the Sherman Act. In reaching this holding, the US court concluded that in analysing the competitive effects of a vertical restraint on a

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"transactional" two-sided platform, effects on the two sides of the platform must be taken into consideration in a single combined assessment.

In other words, it is not sufficient to find an anticompetitive effect on one side of the platform – for example, in the *Amex* case, increased fees to merchants. Instead, proof of a violation requires there to be an overall anticompetitive effect, such as that the 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 Supreme Court cautioned that it is not always necessary to consider both sides of a two-sided platform. Specifically, where the impact of indirect network effects are minor, and the platform does not facilitate a single simultaneous transaction, competitive effects may continue to be analysed separately for each side of the platform.

Four years ago, the decision of the Court of Justice of the European Union in *Groupement des Cartes Bancaires v Commission* focused on the appropriate context for applying the concept of a restriction of competition "by object" rather than "by effect". In so doing, the EU court also addressed whether competitive effects on each side of a multi-sided market need to be considered before condemning challenged conduct.

A group of 11 French banks had adopted three measures, purportedly to increase the number of merchants affiliated with the Cartes Bancaires platform and prevent free-riding.

The Court of Justice concluded that, notwithstanding their potential anticompetitive effect on certain card issuers, the measures could not be condemned as restrictive "by object" unless they were by their very nature anticompetitive. This assessment involves taking into account, among other things, all relevant aspects of the economic and legal context of which the measure forms a part – which may include the interaction between the two sides of a multi-sided platform.

These two judgments, *Amex* and *Cartes Bancaires*, present an opportunity to assess the degree of convergence or divergence, or just the plain difference, in the approaches taken by the highest courts of the US and the EU to an issue that is likely to be of increasing importance in both economies.

US Supreme Court

The US court began its analysis by confirming that the first step in determining whether a vertical restraint, such as the American Express anti-steering provision, violates the rule of reason is for the claimant to demonstrate that the restraint has a substantial anticompetitive effect that harms consumers in the relevant market. The court reiterated

that this initial step may be satisfied by direct evidence of actual detrimental effects on competition, such as reduced output, increased prices or decreased quality in the relevant market; or by indirect evidence, such as proof of market power, plus some evidence that the restraint harms competition. In this case, the government claimants sought to rely exclusively on direct evidence that American Express had raised the fees it charged to merchants over several years.

The court held that defining a relevant market was an essential element in the analysis. In so doing, the court rejected the claimants' argument that evidence of merchant fee increases presented the actual evidence of adverse competitive effects that obviates the need to define a market. The precedent that the claimants cited – the principle that direct evidence makes market definition unnecessary – arose in the context of horizontal agreements between competitors. Here, the challenged restraint was vertical, which the court said often poses no anticompetitive effect in the absence of market power.

With regard to defining the relevant market, the Supreme Court held that credit cards are a two-sided platform because they have indirect network effects, in which price increases on one side of the platform cannot be implemented without risking a feedback loop of not only lower participation on the side with the higher price, but also declining demand on the other side of the platform. Therefore, the increased fees charged to merchants do not necessarily suggest anticompetitive effects absent some evidence that they have increased the overall cost of the platform's services.

The court made clear that two-sided platforms should be analysed as one-sided (ie, without balancing the effects on each side of the platform) when the impacts of indirect network effects and relevant pricing are minor. Only in the context of two-sided transaction platforms, which facilitate a "single, simultaneous transaction" between participants, must competitive effects on either side be weighed together in the context of a single two-sided market.

Viewed in this context, the court held that by focusing on only one side of the two-sided credit-card market, the government's proof of increased merchant fees failed to carry the claimant's burden of proving anticompetitive effects in the relevant market. Here, the court conceded that claimants did offer evidence that American Express had increased the percentage of the purchase price that it charged merchants, and that this entire increase was not offset by expenditures on the cardholder side of the market. But, perhaps clarifying its earlier statement that anticompetitive effects may be demonstrated by increased prices or decreased output or quality, the court explained that "market power is the ability to raise price profitably by restricting output."

By defining a single relevant market to include both sides of a transaction platform, the Supreme Court's holding mandates a broad assessment of economic effects under the rule

of reason, which is likely to have implications for challenged vertical restraints in a range of industries. The majority opinion suggests that other platforms that generate revenues through advertising, such as search engines or other online content sites, will be less likely to be treated as two-sided because they typically do not involve a "single, simultaneous transaction". These platforms are also more likely to be analysed in a more broadly defined relevant market, because they compete against a variety of other media for advertising dollars.

The precise market contexts that will be subject to this two-sided market analysis are yet to be determined. The legacy of the *American Express* ruling will probably be a heavily litigated series of cases that will determine, over the next several years, when it is appropriate to apply a two-sided market analysis to a challenged restraint, and whether output restrictions are to be the sole actionable restriction in the rule of reason context.

Court of Justice of the European Union

In *Cartes Bancaires*, the Court of Justice ruled that the concept of a restriction of competition by object must be interpreted restrictively and can only apply to measures that in themselves reveal a sufficient degree of harm to competition. An object infringement is the rough functional equivalent of a per se offence under US law. It includes the most egregious forms of anticompetitive conduct – known as hard-core restrictions – such as price fixing. Unlike per se offences, object infringements can theoretically be justified by invoking article 101(3) of the Treaty on the Functioning of the European Union, where they give rise to pro-competitive benefits – in practice the likelihood of success is slim.

To determine whether a measure reveals a sufficient degree of harm to competition, the "legal and economic context of which it forms part" must be taken into account. This includes the nature of the goods or services affected, as well as the functioning and structure of the market or markets in question.

The Court of Justice held in *Cartes Bancaires* that the General Court failed to address how the restraints were, by their very nature, anticompetitive; it merely showed how the measures were potentially capable of restricting competition. Moreover, the Court of Justice found that because the General Court acknowledged that the banks' measures sought to establish a certain balance between card-issuing and merchant-acquiring activities, the lower court was at most entitled to infer that those measures had as their object the "imposition of a financial contribution on the members . . . which benefit from the efforts of other members for the purposes of developing the acquisition activities of the system". This object could not, by its very nature, be considered harmful to competition.

The assessment of whether a measure has an anticompetitive object also involves taking into account "all relevant aspects", which may include the interaction of the relevant market with a different related market (ie, the card-issuing and merchant-acquiring sides of

the Cartes Bancaires platform). In this regard, the Court of Justice held that the General Court wrongly concluded that finding that the infringement had taken place in the card-issuing market precluded an analysis of the requirements of balance within the Cartes Bancaires platform between issuing and merchant acquisition activities in the context of article 101.

In doing so, the General Court confused the issue of the definition of the relevant market and that of the legal and economic context, which must be taken into account to determine whether there is an object infringement. Consequently, the lower court overlooked a factor – the multi-sidedness of the Cartes Bancaires platform – that was relevant to the determination of whether the measures had an anticompetitive object.

Logically, if the assessment of whether a measure constitutes an object infringement requires taking into account the multi-sidedness of a platform – because that measure does not in itself reveal a sufficient degree of harm to competition – it should not be treated as an infringement by object. Instead, the Court of Justice held that the assessment of the interaction between the two sides of a platform falls within the examination of the effects of the measure on competition. In *Cartes Bancaires*, this assessment should have included balancing the effects on card-issuing and merchant-acquiring activities.

Multi-sided perspectives on two-sided markets

A key distinction between the approach of the Court of Justice of the European Union and the US Supreme Court to assessing multi-sided platforms is that the EU court's judgment in *Cartes Bancaires* neither set aside the lower court's nor the competition enforcer's assessment that payment systems comprise two distinct product markets: the markets for card issuing and merchant acquiring. Indeed, the General Court was entitled to find an infringement of article 101(1) by object in the issuing market without taking into account the acquiring side of the platform. The error in the General Court's assessment was concluding that the evidence supported an object infringement, where it was clear that the measures sought to establish a balance between card-issuing and merchant-acquiring activities.

For instance, if the restraint that formed the basis of the infringement in *Cartes Bancaires*were a hard-core restriction, such as an agreement that was clearly designed to hinder or block new entrants in the card-issuing market, a finding of an object infringement would have been justified. The requirement to take into account the multi-sidedness of the Cartes Bancaires platform – the contextual analysis – only kicked in where the evidence did not support the inference that the measures constituted an object infringement. This approach was confirmed by the General Court in its second *Cartes Bancaires* judgment, which upheld the European Commission's infringement decision.

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In contrast, the US Supreme Court held that the existence of indirect network effects between the acquiring and the issuing sides of the American Express platform warranted defining a single relevant market that comprised both sides of the platform; and that the claimants needed to demonstrate that anti-steering provisions gave rise to anticompetitive effects within that overall market. It follows that there are fundamental differences between the analytical framework of the EU courts and that of the US Supreme Court.

This difference in approach is further illustrated by the 2012 judgment of the General Court in *MasterCard v Commission*, which also involved a payment card platform. In particular, the General Court rejected the applicants' arguments that the European Commission committed a manifest error of assessment in finding that there was a distinct acquiring market as opposed to a single overall market encompassing the entirety of the four-party system. The argument for defining a "single market" was based on the provision of a single service at the joint demand of cardholders and merchants, akin to the logic of the US Supreme Court in *American Express*. In particular, the General Court conceded that although there are certain forms of interaction between the issuing and the acquiring side, "services provided to cardholders and those provided to merchants can be distinguished and, moreover, cardholders and merchants exert separate competitive pressure on issuing and acquiring banks respectively."

There are differences between the applicable standard of review as regards challenges to the relevant product definition in the US and EU courts. In particular, where the definition of a relevant product market involves complex economic appraisals by the European Commission, the General Court will subject the definition to only a review limited to confirming that the Commission did not commit a manifest error of assessment.

It follows that the General Court in *MasterCard*, unlike the US Supreme Court, did not undertake a full factual assessment of whether the relevant product market had been correctly defined. Moreover, the General Court observed that the definition of the relevant market is of no consequence in article 101 cases, provided that the competition enforcer "has rightly concluded, on the basis of the documents referred to in the contested decision, that the agreement in question distorted competition and was liable to have an appreciable effect on trade between member states".

Nevertheless, the difference in approach to defining the relevant product market had a material corresponding impact on how the US Supreme Court and the EU courts balance anticompetitive effects and pro-competitive efficiencies.

In *American Express*, the definition of a single relevant market comprising card-issuing and merchant-acquiring activities meant that the claimants needed to show that the anti-steering provisions gave rise to a net anticompetitive effect, taking both sides of the market into account.

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In contrast, in MasterCard's appeal to the Court of Justice of the European Union, the EU court held that where restrictive effects have been found in only one market of a multi-sided platform (ie the relevant market) "the advantages flowing from the restrictive measure on a separate but connected market also associated with that system cannot, in themselves, be of such a character as to compensate for the disadvantages resulting from that measure in the absence of any proof of the existence of appreciable objective advantages attributable to that measure in the relevant market". The Court of Justice underlined that this condition applies particularly where the consumers on those markets are not substantially the same. This analytical framework was also applied by the General Court in its second *Cartes Bancaires* judgment.

The dissenting opinion in *American Express* would have looked separately at each side of the two-sided market, a view that would have aligned with the stance of the Court of Justice. As it is, the Court of Justice of the European Union and the US Supreme Court have taken different directions.

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