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## The Two-Sided Market Literature Enriches Traditional Antitrust Analysis

*William H. Rooney and David K. Park*

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The term “two-sided market” sounds strange to the antitrust lawyer’s ear. Antitrust markets typically are not described as having “sides.” They consist of a relevant product or set of products, cover a geographic area, and include transactions between buyers and sellers at a particular level of distribution (e.g., manufacturing, wholesale, retail). Although most market participants buy inputs and sell outputs, they usually buy in the market for the input and sell in the market for the output, not compete in a two-sided market.

Still, the growing and informative literature on two-sided platforms, businesses, and markets has much to offer antitrust law. That literature emphasizes that the demand for otherwise distinct products or services may in fact be linked and that a competitive-effects analysis cannot myopically ignore that linkage. To the extent that the two-sided market literature improves competitive-effects analysis, it improves the fundamental purpose of antitrust law.

This essay briefly discusses the importance of acknowledging linked demand for, and relationships among, otherwise distinct products or services, as recommended by the two-sided market literature, with respect to competitive-effects assessments and market definition. We also observe that recognizing linked demand and interrelationships among products or services facilitates the application of legal rules in antitrust cases.

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## I. Recognizing Linked Demand and Interrelationships among Products or Services Improves Competitive-Effects Analysis and Market Definition

Commentators writing about two-sided markets characterize certain businesses that depend on (and facilitate) the interdependent demand of two or more discrete groups of constituents as two-sided platforms or markets. Rochet and Tirole, for example, define two-sided markets as follows:

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“A market is two-sided if the platform can affect the volume of transactions by charging more to one side of the market and reducing the price paid by the other side by an equal amount; in other words, the price structure matters, and platforms must design it so as to bring both sides on board.”<sup>1</sup>

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Another commentator summarizes the necessary conditions for the emergence of a platform business or market as follows:

- (1) there are two or more distinct groups of customers;
- (2) there are externalities associated with customers A and B becoming connected or coordinated in some fashion; and
- (3) an intermediary is necessary to internalize the externalities created by one group for the other group.<sup>2</sup>

THE OBSERVATION THAT THE PRESENCE OF ONE SET OF CONSTITUENTS MAY AFFECT THE DEMAND OF ANOTHER SET OF CONSTITUENTS IS BOTH TYPICAL OF THE TWO-SIDED MARKET LITERATURE AND USEFUL TO A COMPETITIVE-EFFECTS ASSESSMENT.

Although the two-sided market literature sometimes uses market in more of a business sense than in a technical antitrust sense, the observation that the presence of one set of constituents may affect the demand of another set of constituents is both typical of the two-sided market literature and useful to a competitive-effects assessment.

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1 J.-C. Rochet & J. Tirole, *Two-Sided Markets: A Progress Report*, RAND J. ECON. (Autumn 2006).

2 David S. Evans, *The Antitrust Economics of Multi-Sided Platform Markets*, 20 YALE J. ON REG. 325, 331-34 (2003).

Newspaper competition provides a simple example. Newspapers have (at least) two sets of buyers: readers, who buy news, and advertisers, who buy page space. Both readers and advertisers pay the newspaper a fee for the product that they are buying. Advertisers pay more to newspapers with more readers. Readers, on the other hand, do not pay more to newspapers with more advertisers but with better content, which represents a cost to the newspaper. The newspaper may determine that it can maximize revenue by charging readers very little even for expensive content to maximize the number of readers and attract advertisers. A newspaper may also conclude that advertisers in the aggregate are willing to pay more for page space than readers are willing to pay for content. Asserting that a subscription rate is below the cost of providing content, for example, would omit the important revenue that the newspaper receives from advertisers and overlook that publishers seek to maximize aggregate revenues from readers and advertisers alike.

Capturing competitive effects in a dynamic analytical paradigm also has important implications for market definition. Demand for apparently distinct products may be linked in a way that requires the products to be included in the same competitive venue—or relevant market—for their competitive dynamics to be understood properly. Although courts and agencies typically include in a relevant market products that are substitutes for one another,<sup>3</sup> cluster markets have been defined to include complementary products that respond to linked consumer demands and offer sellers economies of scope. Examples of cluster markets have included such complementary or related product groupings as:

- (1) general acute care inpatient hospital services;<sup>4</sup>
- (2) commercial banking services;<sup>5</sup>
- (3) accredited central station service alarms (including burglar and fire alarm services);<sup>6</sup> and
- (4) small business loans and depository services.<sup>7</sup>

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3 Compare e.g., U.S. Department of Justice and Federal Trade Commission Horizontal Merger Guidelines (the "Horizontal Merger Guidelines") §1.11 (1992, revised 1997) (own-price and cross-product elasticities, and "practical indicia") with *Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962) (reasonable interchangeability of use, cross-product elasticities of demand, and practical indicia) and with *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 395, 400 (1956) (reasonable interchangeability for the same purposes and cross-elasticity of demand across products).

4 *United States v. L.I. Jewish Med. Cen.*, 983 F.Supp. 121, 140 (E.D.N.Y. 1997).

5 *United States v. Phil. Nat'l Bank*, 374 U.S. 321, 356 (1963).

6 *United States v. Grinnell Corp.*, 384 U.S. 563, 572 (1966).

7 See Robert L. Webb, *Divestiture: A Prescription for Healthy Competition*, THE REGIONAL ECONOMIST, Jan. 2001, available at <http://stlouisfed.org/publications/re/2001/a/pages/economic-backgnd.html>.

Further to the cluster-market authorities, the U.S. Court of Appeals for the Ninth Circuit upheld two all-parts markets in *Kodak II* that included all replacement parts for Kodak photocopiers and for Kodak micrographics equipment, respectively.<sup>8</sup> The court in *Kodak II* rejected defendants' argument that "because no two parts are interchangeable, the relevant markets for parts consist of the market for each individual part for Kodak photocopiers and each single part for Kodak micrographics equipment."<sup>9</sup> The Ninth Circuit explained that "Kodak's market definition focuses exclusively on the interchangeability of the parts although ignoring the 'commercial realities' faced by ISOs and end users."<sup>10</sup> The Ninth Circuit cited *Grinnell* and *Philadelphia National Bank* as examples of cases where, after analyzing the commercial realities, the Supreme Court "has held that groups of non-interchangeable products and services may be aggregated to form a single relevant market."<sup>11</sup>

Consumer demand for the deposit, withdrawal, and use of funds provides another example of linked demand for a compound product that is comprised of otherwise apparently distinct components. A bank customer can obtain a compound product—the deposit of funds and the withdrawal funds—from a single supplier (i.e., a bank). That product, however, increases in value when it is provided by multiple suppliers cooperating with one another (i.e., a bank and its network of ATMs). Multiple and diverse suppliers (i.e., a bank, network ATMs, and network merchants) can collaborate to provide consumers with an even more valuable compound product—the deposit and withdrawal of funds and the use of those funds to purchase goods and services from merchants throughout the economy).

Whether all services that facilitate the deposit, withdrawal, and use of funds, and all of the providers of those services, compete in one network market or in multiple markets consisting of only portions of those services poses an interesting question under antitrust law. Although we do not propose to answer that question here, principles from the two-sided market literature imply that the market-definition inquiry may be affected by the practice in question and its competitive context. Such principles suggest that the examination of the competitive objective of the particular practice at issue and the consumer demand to which the practice is intended to respond help identify the venue in which the competitive effects of the practice should be assessed. They further suggest that competitive objective and consumer demand bear on the qualitative analysis of competitive impact, including whether the relevant competition is properly described as intrabrand or interbrand.

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8 *Image Technical Services, Inc. v. Eastman Kodak Co.*, 125 F.3d 1195, 1203 (9th Cir. 1997).

9 *Id.*

10 *Id.*

11 *Id.* at 1204.

## II. Acknowledging Linked Demand Improves the Application of Legal Rules

In *BMI*,<sup>12</sup> the U.S. Supreme Court examined whether the collective pricing of blanket licenses offered to the copyrighted works of songwriter members of ASCAP and BMI constituted per se price-fixing.<sup>13</sup> If the practice were viewed as an agreement among otherwise competing songwriters as to the terms of their respective licenses, the agreement may have been properly viewed as per se illegal. The Court, however, examined the blanket license in competitive context and recognized that the license responded to the demand of radio stations for a bundle of related services and that the collaborating songwriters could not have provided the same product themselves:

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“[h]ere, the whole is truly greater than the sum of its parts; [the blanket license] is, to some extent, a different product. The blanket license has certain unique characteristics: It allows the licensee immediate use of covered compositions, without the delay of prior individual negotiations, and great flexibility in the choice of musical material. ... Thus, to the extent the blanket license is a different product, ASCAP is not really a joint sales agency offering the individual goods of many sellers, but is a separate seller offering its blanket license, of which the individual compositions are raw material. ASCAP, in short, made a market in which individual composers are inherently unable to compete fully effectively.”<sup>14</sup>

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By recognizing that the songwriter members of ASCAP and BMI were collaborating to supply a compound product in response to a linked demand by radio stations, the U.S. Supreme Court declined to declare the blanket license per se illegal.<sup>15</sup> *BMI* has provided important guidance in the last 25 years by instructing courts to review the substance of an arrangement, not its form, and to assess whether alleged co-conspirators are in fact collaborating to satisfy consumer demand more effectively than any one participant could on its own.

The U.S. Supreme Court recently elaborated on its holding in *BMI* to clarify that the legal capacity in which market participants act is determined by the sub-

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12 *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.* (“*BMI*”), 441 U.S. 1 (1979).

13 *Id.* at 4.

14 *Id.* at 21-23 (footnotes omitted).

15 *Id.* at 24.

stance and objective of their concerted activity. In *Dagher*,<sup>16</sup> Texaco Inc. and Shell Oil Co. formed a joint venture called Equilon Enterprises to market their respective gasoline in the western part of the United States.<sup>17</sup> Texaco and Shell Oil maintained their respective brands of gasoline but set the prices of their gasoline jointly through Equilon.<sup>18</sup> Plaintiffs claimed that Equilon provided a vehicle through which Texaco and Shell Oil had engaged in per se illegal price-fixing.<sup>19</sup> The Court, however, characterized the price setting by the joint venture as “little more than price setting by a single entity—albeit within the context of a joint venture [Equilon]—and not a pricing agreement between competing entities with respect to their competing products.”<sup>20</sup>

Further to its holding in *BMI*, the U.S. Supreme Court forcefully rejected the application of the per se rule of illegality to the pricing conduct of Equilon:

BMI HAS PROVIDED IMPORTANT GUIDANCE IN THE LAST 25 YEARS BY INSTRUCTING COURTS TO REVIEW THE SUBSTANCE OF AN ARRANGEMENT, NOT ITS FORM, AND TO ASSESS WHETHER ALLEGED CO-CONSPIRATORS ARE IN FACT COLLABORATING TO SATISFY CONSUMER DEMAND MORE EFFECTIVELY THAN ANY ONE PARTICIPANT COULD ON ITS OWN.

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“When ‘persons who would otherwise be competitors pool their capital and share the risks of loss as well as the opportunities for profit...such joint ventures [are] regarded as a single firm competing with other sellers in the market.’ *Arizona v. Maricopa County Medical Soc.*, 457 U.S. 332, 356 (1982). As such, though Equilon’s pricing policy may be price fixing in a literal sense, it is not price fixing in the antitrust sense. See *Broadcast Music, Inc. v. Columbia Broadcasting System Inc.*, 441 U.S. 1, 9 (1979) (“When two partners set the price of their goods or services they are literally ‘price fixing,’ but they are not *per se* in violation of the Sherman Act”).”<sup>21</sup>

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16 *Texaco Inc. v. Dagher*, 126 S.Ct. 1276 (2006).

17 *Id.* at 1278.

18 *Id.*

19 *Id.* at 1279.

20 *Id.* at 1280.

21 *Id.* (alterations in original).

Although the U.S. Supreme Court formally limited its holding to rejecting the application of the *per se* rule of illegality,<sup>22</sup> it implied that Equilon was a single market participant and that, following the formation of Equilon, Texaco and Shell Oil acted through Equilon not as competitors but as shareholders.<sup>23</sup> Indeed, the Court clarified that the pricing conduct at issue was sufficiently close to the core of the collaboration between Texaco and Shell Oil that such conduct could not be considered a restraint subject to the ancillary-restraints analysis that is fundamental to the application of Section 1 of the Sherman Act: “We agree with petitioners that the ancillary restraints doctrine has no application here, where the business practice being challenged involves the core activity of the joint venture itself—namely, the pricing of the very goods produced and sold by [the joint venture].”<sup>24</sup> The Court therefore found that the price setting neither was *per se* illegal price-fixing nor should be assessed under the ancillary restraints doctrine of Section 1 of the Sherman Act.<sup>25</sup>

*BMI* and *Dahger* reflect the importance of examining the context and objective of the conduct at issue to determine the capacity in which the parties were acting—whether the parties to the restraint were acting as conspiring competitors or collaborating suppliers that formed a single market participant. That examination is also critical to determining whether any residual or incidental competition among the relevant sellers was intrabrand (competition in the sale of the same product) or interbrand (competition in the sale of substitute products). The U.S. Supreme Court has emphasized for almost 30 years, and most recently in *Volvo Trucks North America, Inc. v. Reeder-Simco GMC, Inc.*,<sup>26</sup> that interbrand competition is the primary concern of antitrust enforcement.<sup>27</sup>

In *SCFC ILC, Inc. v. Visa USA, Inc.*,<sup>28</sup> the U.S. Court of Appeals for the Tenth Circuit considered a Visa rule that did not allow Discover (or American

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22 *Id.* at n.2 (noting that “Respondents have not put forth a rule of reason claim.”).

23 *Id.*

24 *Id.* at 1281.

25 *Id.*

26 126 S.Ct. 860, 872-73 (2006).

27 The U.S. Supreme Court defined interbrand and intrabrand competition in *Continental T.V. Inc. v. Sylvania*, 433 U.S. 36, 52 n.19 (1977): “Interbrand competition is the competition among the manufacturers of the same generic product . . . . In contrast, intrabrand competition is the competition between the distributors . . . of the product of a particular manufacturer.”

28 36 F.3d 958 (10th Cir. 1994).



Express) to issue Visa cards.<sup>29</sup> The Tenth Circuit properly began its assessment by identifying the fundamental competitive objective of the market participants and thus the inter-brand competition at issue:

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“In this lawsuit, Sears and Visa USA stipulated “the relevant market is the general purpose charge card market in the United States.” Presently, the only participants in this market are Visa USA, MasterCard, American Express, Citibank (Diners Club and Carte Blanche), and Sears (Discover Card). Competition among these five firms to place their individual credit cards into a customer’s pocket is called *intersystem*. “Interbrand competition is the competition among the manufacturers of the same generic product...and is the primary concern of antitrust law.” *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 52 n.19 (1977).”<sup>30</sup>

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The SCFC court further explained that competition among those collaborating to form the Visa network was properly understood as intrabrand competition.<sup>31</sup> Although issuers and acquirers may compete with each other in the issuance of Visa cards and the acquisition of transactions, that competition was intrabrand when viewed within the context of the primary competitive objective of permitting cardholders to use funds in depository accounts to purchase goods and services throughout the economy:

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“[T]o the extent that Visa USA is in the market, it operates in the *systems* market, not the *issuer* market. Its *members* issue cards, competing with each other to offer better terms or more attractive features for their individual credit card programs. This is *intrasystem* competition.”<sup>32</sup>

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29 The district court notes the language Visa added to its bylaws: “[T]he corporation shall not accept for membership any applicant which is issuing, directly or indirectly, Discover cards or American Express cards, or any other cards deemed competitive...” SCFC ILC, Inc. v. Visa U.S.A., Inc., 819 F.Supp. 956, 964 (D. Utah 1993). Under the bylaw “non-VISA members who develop a successful proprietary card would be prohibited from joining the VISA system and current VISA members would be expelled from the system if they developed such a card.” *Id.* at 966.

30 SCFC ILC, Inc., 36 F.3d at 966 (emphasis added) (internal citations omitted).

31 *Id.* at 967.

32 *Id.* (emphasis added).

### III. Conclusion

The two-sided market literature enriches antitrust analysis by illustrating how consumer demand can require product or service compilations and supplier collaborations that, in other contexts, may present concerns under the Sherman Act. Identifying the competitive objective of the suppliers and the consumer demand to which the suppliers are responding permits a more accurate competitive-effects assessment and market definition and facilitates the application of legal rules, including those prohibiting price-fixing and preserving interbrand competition. ▼