

A big year for business and economics in the courts, even if we're not talking about Janus
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This has been a big year for business in the courts. A U.S. district court approved the AT&T-Time Warner merger, the Supreme Court upheld Amex's agreements with merchants, and a circuit court pushed back on the Federal Trade Commission's vague and heavy handed policing of companies' consumer data safeguards.

These three decisions mark a new era in the intersection of law and economics.

AT&T-Time Warner

AT&T-Time Warner is a *vertical merger*, a combination of firms with a buyer-seller relationship. Time Warner creates and broadcasts content via outlets such as HBO, CNN, and TNT. AT&T distributes content via services such as DirecTV.

Economists see little risk to competition from vertical mergers, although there are some idiosyncratic circumstances in which competition could be harmed. Nevertheless, the U.S. Department of Justice went to court to block the merger.

The last time the government sued to block a merger was more than 40 years ago, and the government lost. Since then, the government relied on the threat of litigation to extract settlements from the merging parties. For example, in the 1996 merger between Time Warner and Turner, the FTC required limits on how the new company could bundle HBO with less desirable channels and eliminated agreements that allowed TCI (a cable company that partially owned Turner) to carry Turner channels at preferential rates.

With AT&T-Time Warner, the government took a big risk, and lost. It was a big risk because (1) it's a vertical merger, and (2) the case against the merger was weak. The government's expert argued consumers would face an extra 45 cents a month on their cable bills if the merger went through, but under cross-examination, conceded it might be as little as 13 cents a month. That's a big difference and raised big questions about the reliability of the expert's model.

Judge Richard J. Leon's 170+ page ruling agreed that the government's case was weak and its expert was not credible. **While it's easy to cheer a victory of big business over big government, the real victory was the judge's heavy reliance on facts, data, and analysis rather than speculation over the potential for consumer harm.** That's a big deal and may make the way for more vertical mergers.

Ohio v. American Express

The Supreme Court's ruling in Amex may seem obscure. The court backed American Express Co.'s policy of preventing retailers from offering customers incentives to pay with cheaper cards.

Amex charges higher fees to merchants than do other cards, such as Visa, MasterCard, and Discover. Amex cardholders also have higher incomes and tend to spend more at stores than those associated with other networks. And, Amex offers its cardholders better benefits, services, and rewards than the other cards. Merchants don't like Amex because of the higher fees, customers prefer Amex because of the card's perks.

Amex, and other card companies, operate in what is known as a *two-sided market*. Put simply, they have two sets of customers: merchants who pay swipe fees, and consumers who pay fees and interest.

Part of Amex's agreement with merchants is an "anti-steering" provision that bars merchants from offering discounts for using non-Amex cards. The U.S. Justice Department and a group of states sued the company, alleging the Amex rules limited merchants' ability to reduce their costs from accepting credit cards, which meant higher retail prices. Amex argued that the higher prices charged to merchants were kicked back to its cardholders in the form of more and better perks.

The Supreme Court found that the Justice Department and states focused exclusively on one side (merchant fees) of the two-sided market. **The courts says the government can't meet its burden by showing *some effect on some part of the market*.** Instead, they must demonstrate, "increased cost of credit card transactions ... reduced number of credit card transactions, or otherwise stifled competition." The government could not prove any of those things.

We live in a world two-sided markets. Amazon may be the biggest two-sided market in the history of the world, linking buyers and sellers. Smartphones such as iPhones and Android devices are two-sided markets, linking consumers with app developers. The Supreme Court's ruling in Amex sets a standard for how antitrust law should treat the economics of two-sided markets.

LabMD

LabMD is another matter that seems obscure, but could have big impacts on the administrative state.

Since the early 2000s, the FTC has brought charges against more than 150 companies alleging they had bad security or privacy practices. LabMD was one of them, when its computer system was compromised by professional hackers in 2008. The FTC claimed that LabMD's failure to adequately protect customer data was an "unfair" business practice.

Challenging the FTC can get very expensive and the agency used the threat of litigation to secure settlements from dozens of companies. It then used those settlements to convince everyone else that those settlements constituted binding law and enforceable security standards.

Because no one ever forced the FTC to defend what it was doing in court, the FTC's assertion of legal authority became a self-fulfilling prophecy. LabMD, however, chose to challenge the FTC. The fight drove LabMD out of business, but public interest law firm Cause of Action and lawyers at Ropes & Gray took the case on a pro bono basis.

The 11th Circuit Court of Appeals ruled the FTC's approach to developing security standards violates basic principles of due process. **The court said the FTC's basic approach—in which the FTC tries to improve general security practices by suing companies that experience security breaches—violates the basic legal principle that the government can't punish someone for conduct that the government hasn't previously explained is problematic.**

My colleague at ICLE [observes](#) the lesson to learn from LabMD isn't about the illegitimacy of the FTC's approach to internet privacy and security. Instead, it says legality of the administrative state is premised on courts placing a check on abusive regulators.

The lessons learned from these three recent cases reflect a profound shift in thinking about the laws governing economic activity:

- AT&T-Time Warner indicates that facts matter. Mere speculation of potential harms will not satisfy the court.
- Amex highlights the growing role two-sided markets play in our economy and provides framework for evaluating competition in these markets.
- LabMD is a small step in reining in the administrative state. Regulations must be scrutinized before they are imposed and enforced.

In some ways none of these decisions are revolutionary. Instead, they reflect an evolution toward greater transparency in how the law is to be applied and greater scrutiny over how the regulations are imposed.

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