

Amazon — The 1st Illegal Monopsony?

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It's been nearly four months since the New York Times first published reports of deteriorating contract negotiations between Amazon.com Inc. and Hachette Book Group. [1] While some details have begun to trickle in from the online retailer and book publisher, not much has been divulged with respect to the exact nature of the dispute. The general consensus is that Hachette prefers to return to an agency pricing model, which allows publishers to set the prices of their own books. Amazon is adamantly opposed to this switch because the agency model prevents the kind of drastic discounting that Amazon is known for. All of this has ignited commentary among authors, publishers and observers alike. It's no secret that publishers deem Amazon's discounting practices and bullying tactics a violation of antitrust laws. Recent debate, however, has focused on whether U.S. regulators tend to agree.



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The State Of Affairs

Do you recall that other much-publicized dispute over e-book prices circa 2012-2013? In a high-profile trial, the U.S. Department of Justice successfully claimed that the six largest publishers in the U.S., including Hachette, unlawfully colluded with Apple Inc. to raise e-book prices by introducing the agency pricing model in response to Amazon's deep discounting.[2] The publishers settled the case and agreed to certain restrictions, which largely enabled Amazon to continue discounting e-books. Moreover, U.S. District Judge Denise Cote's final order, issued in 2013, laid out a staggered schedule for the various publishers to renegotiate their contracts with retailers.[3] As it turns out, Hachette was up first.

It's been reported that negotiations rapidly deteriorated when Amazon demanded better terms from Hachette and Hachette refused.[4] Amazon retaliated by declaring literary war on Hachette in an effort to force the publisher's hand. Specifically, Amazon delayed delivery of books published by Hachette for up to three weeks, removed the pre-order option for Hachette titles, charged more for Hachette books, and even suggested that readers might enjoy a book from another publisher instead.

To add to the hype, Hachette authors simultaneously took to social media to denounce the mammoth online retailer for offenses ranging from bullying to extortion to a violation of antitrust laws. Political satirist, television host and Hachette author Stephen Colbert even started an "I Didn't Buy It On Amazon" sticker campaign. Colbert encouraged readers to put the sticker on their books in a show of solidarity. Needless to say, the Internet has been abuzz ever since.

Then the “United” campaigns started. First up, in early August, 900 authors signed a letter encouraging authors to email Jeff Bezos, CEO of Amazon, to tell him “in the strongest possible terms” to stop harming the livelihood of authors by holding books hostage.[5] The letter, published under the name “Authors United,” ran in a full-page ad in the New York Times. In response, Amazon launched ReadersUnited.com to publish a letter from the Amazon Books Team, which pitches itself as a champion for readers. [6] Amazon’s letter encourages readers to contact Hachette’s CEO, Michael Pietsch. Suggested talking points: “We have noted your illegal collusion. Please stop working so hard to overcharge for ebooks. They can and should be less expensive.” (Direct, and to the point.)

Meanwhile, across the pond, more than 1,000 authors from Germany, Austria and Switzerland took a page from the Authors United movement and signed a similar open letter to Amazon accusing the online retailer of using improper tactics in a dispute over e-book prices with Bonnier AB, a German publishing trade group. In June, Bonnier filed a complaint with German competition authorities claiming that Amazon delayed delivery of its books in order to force the publisher to accept lower prices for its e-books.[7] Reportedly, the European Commission has begun a preliminary investigation into Bonnier’s allegations.[8] European competition law expressly forbids companies with a dominant market position from engaging in abusive conduct.

Monopoly, Monopsony — What’s The Difference?

Despite the buzz, as of the date of this article, no publisher or author has filed a lawsuit against Amazon for antitrust violations. While commentators often attach the word “monopoly” to Amazon, the real inquiry is whether Amazon is, instead, a “monopsony.” An unlawful monopsony, the lesser known violation in the antitrust family, occurs when a buyer of goods has the power to unlawfully lower the prices of the products that it buys. By contrast, an unlawful monopoly occurs when a seller of goods has the power to unlawfully raise the prices of what it sells. Both result in a misallocation of resources, which harms consumers and distorts markets, and therefore each violates antitrust law.

The theory of monopsony assumes that the monopsonist has the power to dictate terms to its suppliers. However, to show monopsony, one must show that suppliers are forced to sell their products at prices so low that the loss results in a reduction of supply. Harm to the market results when suppliers are, in turn, driven out of business, or have less money to invest in new innovation, technology, equipment and/or expansion. In that sense, a monopsony often does not directly affect consumers in the traditional way that unlawful monopolies do.

As an added wrinkle, buyer power without actual monopsony power can actually benefit consumers. Indeed, when buyer power pushes prices down without resulting supply reduction, consumers enjoy lower prices. Consumers are harmed, however, when output reduction is coupled with a misallocation of resources. While consumers may not immediately feel the effects of the monopsony, harm resonates nonetheless as wealth is transferred to the monopsonist, and consumers are ultimately faced with higher prices and fewer options.

For its part, Amazon has a strong reputation for consumer-friendly discounting. Thus, as consumers enjoy discounted e-book prices, it is difficult to imagine how they are monetarily harmed by Amazon’s practices. The relevant question is whether Amazon’s bullying tactics with publishers could effectively result in a reduction of books being published.

Will Amazon Be The First Illegal Monopsony?

Significantly, no U.S. court has yet to find a single company guilty of an unlawful monopsony. The case that came the closest was *Weyerhaeuser Co. v. Ross-Simmons Hardware Lumber Co.*[9] In *Weyerhaeuser*, a dominant purchaser of logs was accused of overbidding, and driving its smaller rival out of business.[10] While the trial court and Ninth Circuit found for the plaintiffs, agreeing that the defendant engaged in anti-competitive conduct by overbidding for logs, the U.S. Supreme Court reversed 9-0.[11]

The *Weyerhaeuser* court concluded that predatory buying must be evaluated under a much stricter analysis than that contemplated by the Ninth Circuit.[12] Specifically, the court held that a buyer is liable only if (1) buy-side bidding caused costs to rise higher than revenues, and (2) the defendant has a “dangerous probability of recouping the losses” through an “exercise of monopsony power.”[13] It is important to note that under the *Weyerhaeuser* standard, recoupment of costs via higher prices in the downstream market does not satisfy the test. Rather, the Supreme Court required recoupment “through the exercise of monopsony power,” that is — by forcing lower prices on the buy-side.[14]

Since Amazon first introduced its Kindle product, it has priced e-books below its cost of purchasing them. For example, if Amazon bought an e-book from Hachette for \$15, it resold it to a consumer for \$9.99, losing \$5.01 per e-book. Not surprisingly, e-book consumers flocked to Amazon helping the online retailer to grow exponentially over the years, and causing publishers and authors to rely on Amazon’s sales. In fact, some have even suggested that consumers use Amazon as a modern-day card catalog. According to that theory, if a book or author is not sold on Amazon, that book or author does not exist.

With its low prices and established reputation as a consumer-friendly reading room of sorts, there is little debate that Amazon is a dominating force in the e-book market, both on the buy-side and sell-side. Reports place Amazon’s share of the e-books market around 60 percent.[15] Moreover, Amazon accounts for nearly 65 percent of Hachette’s e-book sales. Thus, Amazon certainly has market power in the antitrust sense, and its buyer power alone cannot be said to be merely circumstantial.

Now it seems that Amazon is attempting to enhance its bottom line by wielding its power in the market to achieve more favorable pricing from publishers, rather than by increasing its own prices downstream, i.e., recoupment through the exercise of monopsony power. It remains to be seen, however, whether Amazon’s tactics will result in a reduction of output. Publishers will certainly feel the monetary effects of expensive services and larger discounts paid to Amazon. Likewise, Authors will suffer if publishers are unable to pay large advances, or if they are are paid less per book due to higher discounts paid to Amazon.

In just a few keystrokes, Amazon has the ability to curb a book’s commercial success, and impact an author’s achievements. While literary giants, and Hachette authors, like Stephen King, James Patterson and J.K. Rowling will likely be able to ride out the storm, lesser known and debut authors may struggle or become extinct. Stifling authors will lead to fewer publications for consumers to choose from, and a reallocation of wealth flowing directly to Amazon.

Interestingly, in an effort to break its standoff with Hachette, Amazon executive David Naggar, wrote an open letter to Hachette authors proposing to take them out of the middle of the dispute by promising them 100 percent of the sales price of every Hachette e-book sold on Amazon.[16] Unsurprisingly, Hachette quickly rejected the proposal. Whether Amazon is trying to avoid being labeled an unlawful monopsonist by this recent proposal, or whether it is just trying to win back the hearts of frustrated

authors and consumers remains to be seen.

Conclusion

All of this has led many to ponder whether Amazon's recent exploits might (finally) raise the eyebrows of U.S. antitrust watchdogs. Some antitrust analysts believe that it is premature to go after Amazon at this stage, and the general consensus among most is that U.S. regulators are not likely to intervene. Others view this dispute as ordinary business dealings between a retailer and supplier, and maintain that the enormous attention merely stems from the visibility and notoriety of the parties involved. Further, U.S. antitrust authorities have historically prioritized Amazon's treatment of consumers over the pressure it puts on suppliers. However, as Amazon becomes increasingly willing to withhold products from consumers in order to apply pressure on suppliers for better terms and greater discounts, it is certain that U.S. regulators and others will be watching closely.

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[1] David Streitfeld, Hachette Says Amazon Is Delaying Delivery of Some Books, N.Y. Times, May 8, 2014, <http://www.nytimes.com/2014/05/09/technology/hachette-says-amazon-is-delaying-delivery-of-some-books.html>.

[2] Opinion & Order, U.S. v. Apple, Inc., 12-cv-02826 (S.D.N.Y. July 10, 2013), available at <http://www.justice.gov/atr/cases/f299200/299275.pdf>.

[3] Final Judgment, U.S. v. Apple, Inc., 12-cv-02826 (S.D.N.Y. Sept. 5, 2013), available at <http://www.justice.gov/atr/cases/f300500/300510.pdf>.

[4] David Streitfeld, Hachette Says Amazon Is Delaying Delivery of Some Books, N.Y. Times, May 8, 2014, <http://www.nytimes.com/2014/05/09/technology/hachette-says-amazon-is-delaying-delivery-of-some-books.html>.

[5] A Letter to Our Readers, <http://www.authorsunited.net/>

[6] A Message from the Amazon Books Team, <http://www.readersunited.com/>

[7] Press Release, Federation of European Publishers, German Publishers and Booksellers Association Files Complaint with the Bundeskartellamt against Amazon, June 24, 2014, <http://www.fep-fee.eu/Press-release-German-Publishers>

[8] Press Release, Federation of European Publishers, Antitrust Complaint against Amazon: Börsenverein Welcomes EU Commission's Preliminary Investigation, July 11, 2014, <http://www.fep-fee.eu/Antitrust-Complaint-against-Amazon>

[9] 549 U.S. 312 (2007).

[10] Id.

[11] Confederated Tribes of Siletz Indians of Or. v. Weyerhaeuser Co., 411 F.3d 1030 (9th Cir. 2004); Weyerhaeuser, 549 U.S. 312 (2007).

[12] Weyerhaeuser, 549 U.S. at 325-326.

[13] Id.

[14] Id. at 325.

[15] Reed Stevenson and Jing Cao, Amazon Calls for E-Book Price Cuts Amid Hachette Dispute, Bloomberg, July 30, 2014, <http://www.bloomberg.com/news/2014-07-29/amazon-makes-case-for-lower-e-book-prices-amid-hachette-dispute.html>

[16] David Streitfeld, Amazon Angles to Attract Hachette's Authors to Its Side, N.Y. Times, July 8, 2014, <http://bits.blogs.nytimes.com/2014/07/08/amazon-tries-to-woo-authors-in-hachette-dispute/>.

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