

CLIENT ALERT

Genuine Product Improvement Not Monopolization, California Jury Finds in Closely Watched Apple iPod Trial

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After nine years of litigation and a two-week trial, a California federal jury took all of three hours to find that an Apple iTunes software update in 2006 was a genuine product improvement, and therefore not an antitrust violation. Technology firms have long watched the case for guidance on the extent to which the antitrust laws require manufacturers to make their products interoperable with downstream content provided by third parties in the face of countervailing security and data rights concerns. Here, the jury found that interoperability was not mandatory.

The plaintiffs—purporting to represent a class of at least eight million Apple iPod owners—alleged that an Apple software update that prevented iPod users from uploading songs from third-party sellers onto their devices, had enabled Apple to monopolize digital music. The trial gained national attention outside antitrust circles when late Apple co-founder and former CEO Steve Jobs testified by a taped video deposition.

Apple's release of iTunes 7.0 disabled a user's iPod if it detected songs from music stores other than Apple's iTunes store. The update also prevented songs purchased on iTunes from being used on rival digital music players. At the time, Apple controlled approximately 70 percent of all online music sales.

The plaintiffs argued that Apple was blocking songs from rival online music retailers and preventing users from listening to iTunes songs on other devices to raise the price of iPods. The plaintiffs' expert testified that Apple's actions allowed Apple to maintain a monopoly over digital music and charge approximately \$16 more per iPod, a nearly 7.5 percent increase. In defense, Apple argued that the digital rights restriction was never intended to harm competitors, but instead to protect iPods from being hacked. Apple also argued that content owners were requiring this more stringent digital rights management technology.

U.S. District Court Judge Yvonne Gonzalez Rogers bifurcated the issues presented at trial so that the jury would first determine whether iTunes 7.0 was a genuine product improvement or a subterfuge to charge monopoly prices. Importantly, in her jury instructions, Judge Gonzalez Rogers cautioned that "a company has no general legal duty to assist its competitors, including by making its products interoperable, licensing to competitors, or sharing information with its competitors." The jury quickly found in Apple's favor.

Other issues in the long-running litigation that had received attention in antitrust circles were not resolved. For example, the jury did not reach a finding on whether Apple possessed monopoly power in a relevant antitrust market—either portable music devices or digital music. Apple had argued that the plaintiffs' theory was limited to perfect substitutes in the device market—ignoring imperfect substitutes. Indeed, this argument echoes analysis by the Department of Justice in its March 2008 decision not to challenge the merger between satellite radio providers Sirius and XM. One of the reasons the DOJ concluded that proposed merger was unlikely to enable a price increase was the multiple competitive alternatives for audio entertainment, including Internet radio, high definition radio, portable music players (such as iPods), and music-enabled cellular phones. More broadly, the DOJ also noted the development of various new technology platforms—especially rapidly evolving mobile devices—

and that a "significant number of consumers in the future are likely to consider one or more of these platforms as an attractive alternative to satellite radio." And in due course, after the blockbuster success of its phone and tablet product lines, Apple did in fact discontinue sales of the iPod altogether.

The Apple trial result may stimulate the development and maintenance of closed ecosystems and reduce concern that interoperability is required by the antitrust laws, particularly if the update can be characterized as a genuine product improvement. The plaintiffs plan to appeal the jury's verdict. Post-trial motions, appeals, and agency signals coming out of this verdict should be watched closely, as should related cases like the multidistrict litigation involving Keurig brand coffee makers and Green Mountain Coffee Roasters.

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