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Ninth Circuit Courts Reject Antitrust "Bundling" Claims In Two Recent Cases

In two recent cases, federal courts in the Ninth Circuit rejected plaintiffs' claims that alleged "bundling" practices violated the antitrust laws. In the first, *Masimo* v. *Tyco Health Care Group, L.P.*, the Ninth Circuit Court of Appeals held that a competitor-plaintiff could not maintain an action based on the defendant's bundled discounts on certain medical devices where plaintiff had failed to allege (or prove) either that such discounts were predatory or that they foreclosed competition in the relevant market.[1] In the second, *Brantley* v. *NBC Universal, Inc.*, the United States District Court for Central District of California dismissed a class action complaint alleging that distributors and programmers of cable television content unlawfully bundled such content because plaintiffs had failed to allege foreclosure of any actual or potential competition.[2] These cases further clarify the standards that courts in the Ninth Circuit, and potentially elsewhere, apply to claims that bundling practices of various kinds are anticompetitive.

Masimo involved claims by a competitor, Masimo, challenging certain of Tyco's business practices in the market for pulse oximetry products – medical devices used to measure heart and lung functions. On October 28, 2009, the Ninth Circuit Court of Appeals upheld a district court decision that vacated in part a jury's verdict against Tyco, and ruled that Masimo's claims regarding Tyco's bundled discounting practices failed as a matter of law. As an initial matter, the Court of Appeals reaffirmed its holding in *Cascade Health Solutions* v. *PeaceHealth*, that bundled discounts – which involve offering a bundle of two or more goods or services at a lower price than the seller charges for such goods or services purchased individually – do not violate section 2 of the Sherman Act "unless the discounts result in prices that are below an appropriate measure of the defendant's costs."[3] In *PeaceHealth*, the Ninth Circuit observed that bundled discounts generally benefit consumers because they allow the buyer "to get more for less." The court adopted a discount attribution standard to identify those bundling strategies that involve pricing below an appropriate measure of cost – and therefore are more likely to cause harm to competition in the long run.[4] Under that standard, the discounts given by the defendant on the bundle are allocated to the product that is subject to competition from other producers. If the resulting price of the competitive product is below the defendant's cost to produce it, the bundled

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1 Nos. 07-55960, 07-56017, 2009 WL 3451725 (9th Cir. Oct. 28, 2009).

2 No. CV07-06101 (C.D. Cal. Oct. 15, 2009).

3 *Cascade Health Solutions* v. *PeaceHealth*, 515 F.3d 883, 903 (9th Cir. 2008).

4 *Id.* at 895.

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discount may be considered exclusionary.[5] Following *PeaceHealth*, the court in *Masimo* held that – notwithstanding a jury verdict that Tyco's bundled discounts on pulse oximetry products were unlawful – the plaintiff did not even allege that Tyco's bundled pricing fell below an appropriate measure of cost. The court concluded, therefore, such discounts could not, as a matter of law, violate section 2.[6]

The *Masimo* court noted, however, that *PeaceHealth* left open the possibility that application of the discount attribution test may be inappropriate outside the context of bundled discounting – "'for example, in tying or exclusive dealing cases.'"[7] Masimo's claim, the court determined, was that Tyco's bundling practices were actually market-share discounts, conditioned upon customers purchasing nearly all their requirements for products in the bundle (which included pulse oximetry and other unrelated products) from Tyco. As such, the discounts arguably constituted exclusive dealing arrangements, designed to prevent Tyco's customers from purchasing the goods in the bundle from competitors. Nonetheless, the court held that the jury's verdicts of liability with respect to such practices could not be sustained because Masimo had failed to prove that Tyco's bundling practices "foreclosed competition in a substantial share of the relevant market."[8]

As to Masimo's claims that Tyco entered into exclusive dealing arrangements in the form of sole source and market share agreements that violated the antitrust laws, the court held that the District Court had properly upheld the jury's findings of liability. The District Court had held that a reasonable jury could conclude that Tyco's agreements with hospitals and group purchasing organizations were exclusive and resulted in substantial foreclosure in the market, and could also conclude that the effects of the foreclosure outweighed the procompetitive effects of the agreements and discounts offered in those agreements.[9] The Ninth Circuit concluded that none of the arguments proffered by Tyco on this issue compelled reversal.

Brantley v. *NBC Universal* involved a class action complaint brought on behalf of cable television subscribers alleging that NBC Universal and various other cable programmers and distributors conspired to limit competition and maintain premium prices by offering only bundled programming to consumers. On October 15, 2009, the District Court granted the defendants' motion to dismiss the complaint with prejudice, holding that plaintiffs had failed to state a claim under the antitrust laws. Whereas *Masimo* primarily concerned claims brought under section 2 of the Sherman Act, *Brantley* concerned allegations that the cable programmer and distributor defendants had entered into vertical agreements to limit competition in violation of section 1.

Specifically, plaintiffs' complaint in *Brantley* alleged that, to avoid competition and extract premium prices, video programmers offered to sell or license content to cable and satellite distributors only on a "bundled" basis; in turn, the distributors offered to consumers only "prepackaged bundled tiers" of programming, rather than individual channels.[10] The District

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5 *Id.* at 906.

6 *Masimo*, 2009 WL 3451725, at *1.

7 *Id.* (quoting *PeaceHealth*, 515 F.3d at 916 n.27).

8 *Id.* at *2.

9 *Masimo Corp.* v. *Tyco Health Care Group, L.P.*, 2006 WL 1236666, *5-8 (C.D.Cal. March 22, 2006).

10 Order, No. CV07-06101, at 2.

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Court treated these allegations – which did not involve discounting practices – as amounting to a "tying" claim.[11] Consistent with the holding of the Court of Appeals in *Masimo*, the *Brantley* court rejected plaintiffs' argument that they were not required to show evidence of foreclosure in a substantial share of the market in tying cases and that their allegations of higher prices combined with a deprivation of consumer choice were sufficient to state a claim under section 1. To the contrary, the court held that "any claim of tying or bundling requires foreclosure of actual or potential competition."[12] Because plaintiffs had failed to allege that any actual or potential competitors were excluded from the relevant market, their claims failed as a matter of law.

The plaintiffs in *Brantley* have announced that they will take an immediate appeal of the District Court's decision, which dismissed their complaint with prejudice. It remains to be seen how the Ninth Circuit will rule in that case. The Ninth Circuit's decision in *Masimo* suggests that for claims involving bundling practices where the discount attribution test is not applicable – such as tying and exclusive dealing – proof that the challenged practices foreclose competition in a substantial portion of the market will be required. More broadly, both recent cases indicate that courts in the Ninth Circuit – and, potentially, in other parts of the country – will continue to approach claims that bundled pricing violates the antitrust laws with some skepticism, and with "a measured concern to leave unhampered pricing practices that might benefit consumers, absent the clearest showing that an injury to the competitive process will result."[13]

* * *

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues discussed in this memorandum may be addressed to any of the following:

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[11] *See id.* at 14-15.

[12] *Id.* at 15.

[13] *Masimo*, 2009 WL 3451725, at *1 (quoting *PeaceHealth*, 515 F.3d at 902).