New York Law Journal
SERVING THE BENCH AND BAR SINCE 1888
WWW.NYLJ.COM
An ALM Publication
VOLUME 256—NO. 113
TUESDAY, DECEMBER 13, 2016

ANTITRUST TRADE AND PRACTICE

Expert Analysis

Creative Destruction, Uber and Antitrust

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Sometimes "competition takes the form of 'creative destruction,' whereby an innovator uses a new technology or business model to transform an industry."[1] For example, Apple's iPod revolutionized the portable music market and quickly eliminated compact discs from competition. This innovative competition can push markets forward and force companies to adapt to new, challenging problems—all to the benefit of consumers. However, fear of creative destruction can lead existing competitors to oppose the disruptive innovator. Uber is a recent example of this type of response in the vehicle-for-hire industry. Since entering the market in 2009, Uber has run into frequent opposition from taxi associations and local governments, which in turn has spawned several interesting antitrust disputes.

Two recent decisions, *Wallen v. St. Louis Metropolitan Cab Commission*[2] and *Meyer v. Kalanick*,[3] reflect some of the antitrust issues facing Uber in these battles with incumbents. In *Wallen*, Uber is fighting against a local agency that has sought to prevent Uber from operating in St. Louis. In *Meyer*, Uber is working to justify its business model and pricing algorithms against charges of anticompetitive price-fixing. Below are summaries of the denials of the motions to dismiss in both cases and the antitrust implications raised by the decisions.

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'Wallen'

Last year, many expected Uber's lawsuit in Wallen to test the implications of the Supreme Court's decision in *N.C. Dental*,[4] which held that state agencies are not entitled to state-action immunity unless they can show a clear articulation of state authority and active supervision by the state. This year, the Wallen court's denial of the Metropolitan Taxicab Commission of St. Louis's (MTC) motion to dismiss handed Uber a victory in its drive to defeat claims of antitrust immunity by state agencies. The MTC argued that it could permissibly exclude Uber from the St. Louis market of for-hire transportation because the state-action doctrine made it immune from antitrust scrutiny under *Parker v. Brown* holding that the Sherman Act's antitrust laws do not apply to state actors.[5] To evaluate this argument, the court applied the two-part test from *N.C. Dental*—clear articulation of state authority and active supervision by the state.

Clear Articulation of State Authority. Before analyzing whether the state of Missouri had articulated a clear policy to permit the MTC's conduct, the court noted that the Missouri Legislature created the MTC "for the public purposes of recognizing the taxicab service as a public transportation system, improving the quality of the system, and exercising primary authority over the provision of licensing, control and

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regulations of taxicab services within the district."[6]

The Eastern District of Missouri held that this authority to regulate and oversee vehicles for hire could not justify the MTC's exclusion of Uber: "the displacement of competition is not the logical result of the statutory framework, rather, the logical result is providing a public transportation system that is safe and efficient." Thus, because there was no clear policy to permit Uber's exclusion, the MTC was not immune from antitrust scrutiny and the court denied the MTC's motion to dismiss.

Active Supervision. Because the court found no clear articulation, , it did not address the active supervision prong of the N.C. Dental test.[7] However, active supervision could be at issue in similar cases going forward. In *Wallen*, the MTC's enabling statute required only four of the nine commissioners to be licensed taxi drivers, owners or operators.[8] This suggested that as a simple matter of numbers, non-competitors were supervising the MTC.

Uber, however, argued that instead of adopting a "purely numerical approach to [the issue of] control," the court should focus on practical control of the MTC.[9] This would shift the consideration to whether the non-industry commissioners had strong ties to the taxicab industry or whether the taxi-connected commissioners act together in taking specific MTC actions. Going forward, Uber and similar "disruptors" will likely continue to oppose a purely numerical approach to the active supervision issue.

'Meyer'

Unlike in *Wallen*, Uber suffered a setback in *Meyer* as the court denied its motion to dismiss. In *Meyer*, a former Uber driver alleged that Uber's CEO "conspired" with Uber's drivers to use the company's pricing algorithms[10] to fix ride prices in violation of the Sherman Act. The plaintiff alleged that the putative class members suffered antitrust injury because their fares would have been lower, and output would have been higher, without Uber's pricing algorithms.

For those unfamiliar with Uber's business model, Uber provides a smartphone application platform to match consumers and drivers. In practical terms, Uber sits in the middle, interacting with drivers for "supply" and collecting payment from consumers on the "demand" side.

At the motion to dismiss stage, defendant did not focus on whether Uber and its driver partners should be viewed as integral parts of a legitimate collaboration and therefore free to participate in the setting of the price of the venture's product—an Uber ride—without judicial second-guessing. Instead, defendant focused on market definition as well as the lack of a plausible horizontal conspiracy, which would be subject to per se liability, as opposed to standard vertical arguments, subject to the rule of reason. Perhaps because of that context, the district court treated Uber's business model with skepticism and denied the motion to dismiss.[11] Uber later was joined as a necessary party and the case was stayed pending the Second Circuit's review of Uber's motion to compel arbitration. Two aspects of the court's motion to dismiss decision will be of interest if the case moves forward in the district court: market definition and treatment of Uber's procompetitive justifications.

Market Definition. The district court accepted as plausible plaintiffs' narrow market definition of the "mobile app-generated ride-share service market." Defendant protested that this improperly omitted various substitutes for Uber, such as taxis, public transit and walking. The court, however, stressed the fact-intensive nature of the market definition inquiry and highlighted the plaintiff's allegation that Uber does not compete with taxis. With such a narrowly defined market, Uber was alleged to have an approximately 80 percent market share.

If and when this case moves forward, the court will have to consider the Second Circuit's recent guidance in *U.S. v. American Exp. Co.*[12] regarding the need to consider the entire market when analyzing a "two-sided" platform or market. A two-sided market exists where two or more distinct groups of market participants are connected through a single platform. Uber in particular has been identified as such a platform because it contracts with both drivers and customers and decides how to balance the two sides in determining the prices to charge (or the prices it permits to be charged). Relying on *AmEx*, Uber should be able to argue that the court must consider the two-sided features of the platform when considering the bounds of the overall market at issue.

Procompetitive Justifications. The Meyer court found the plaintiff's allegations that Uber's surge pricing algorithm reduces demand for rides plausible enough to survive the motion to dismiss.[13] However, as the court noted, one could also argue that Uber's surge pricing algorithm does not reduce output, but rather

increases the supply of transportation options available to consumers by incentivizing drivers to use Uber at times of low supply: when more people desire a ride, the algorithm increases the fare prices to attract more drivers until the price falls to a new level.

In this sense, like in many two-sided markets, the price is a reflection of demand and Uber uses its algorithms to determine where supply will best enable the market to be "cleared." It was just this dynamic that had the FTC recognize Uber's platform as an "innovative form of competition" that has increased consumer welfare.[14] Whether the Meyer court would see it this way at summary judgment is yet to be determined.

Stay Tuned

The decisions in *Wallen* and *Meyer* provide an early window into some of the emerging antitrust battles for Uber. In particular, the early decision in *Meyer* is at odds with the FTC's views on disruptive competition. FTC Commissioner Maureen Ohlhausen has noted the positive potential of creative destruction, stating, "disruptive innovation can often bring meaningful change to people's lives."[15] Additionally, former FTC Commissioner and head of President-elect Donald Trump's FTC transition team, Joshua Wright, believes that regulation should "enable these various kinds of competition and not directly or indirectly restrict the introduction or use of new types of applications or the novel features they may provide absent some significant evidence of public harm."[16]

And, most recently, a court in the Eastern District of Pennsylvania accepted this line of reasoning, dismissing a complaint against Uber because it "failed to alert t[he] Court of any negative impact Uber's presence in the marketplace has had on the price, quality, or quantity of taxicab or vehicle-for-hire services—essential indications of antitrust injury."[17]

With Wright leading the FTC's transition team, one can assume that the agencies will continue to be receptive to this form of innovation—however disruptive to competitors—absent significant evidence of likely harm to consumers.

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1. Joshua D. Wright, "Has the D.C. cab commission forgotten who it serves?" WASHINGTON POST (Sept. 6, 2013), https://www.washingtonpost.com/opinions/has-the-dc-cab-commission-forgotten-who-it-serves/2013/09/06/cb-3d0c18-15a6-11e3-be6e-dc6ae8a5b3a8_story.html?utm_term=.4128057f1726.

2. *Wallen v. St. Louis Metro. Taxicab Comm'n*, No. 4:15CV1432 HEA, 2016 WL 5846825 (E.D. Mo. Oct. 6, 2016).

3. *Meyer v. Kalanick*, 174 F. Supp. 3d 817 (S.D.N.Y. 2016), reconsideration denied in part, No. 15 CIV. 9796, 2016 WL 2659591 (S.D.N.Y. May 9, 2016).

4. *North Carolina State Board of Dental Examiners v. F.T.C.*, 135 S. Ct. 1101, 191 L. Ed. 2d 35 (2015).

5. *Parker v. Brown*, 317 U.S. 341, 63 S. Ct. 307, 87 L. Ed. 315 (1943).

6. Mo. Ann. Stat. § 67.1804 (West).

7. Similarly, the active supervision prong was not addressed in *N.C. Dental*. See *N.C. Dental* at 1108.

8. Mo. Ann. Stat. section 67. 1806 (West).

9. Opposition to Motion to Dismiss, *Wallen v. St. Louis Metro. Taxicab Commission*, 2015 WL 10013292 (E.D. Mo. Nov. 6, 2015).

10. Through its surge pricing algorithm, Uber charges higher prices during times of high demand.

11. *Meyer v. Kalanick*, No. 15 CIV. 9796, 2016 WL 4491758 (S.D.N.Y. Aug. 26, 2016) ("The fact that Uber goes to such lengths to portray itself—one might even say disguise itself—as the mere purveyor of an 'app' cannot shield it from the consequences of its operating as much more.").

12. *U.S. v. American Exp. Co.*, No. 15-1672, 2016 WL 5349734 (2d Cir. Sept. 26, 2016) (holding that the district court erred by considering only one side of a "two-sided" credit card market).

13. The court also quickly rejected Uber's CEO's free-riding argument. See *Kalanick*, 2016 WL 4491758 at *6 ("[T]he Court's attention has not been drawn to concerns about free-riding Uber drivers, or to efforts that Uber drivers could make to promote the App that will be under-provided if Uber does not set a pricing algorithm."). However, Uber's driver contracts are non-exclusive, which means that Uber drivers can also drive for taxi companies (that now have app platforms), traditional car service companies or competing app-based platforms such as Lyft. One would think that Uber drivers should not be permitted to use Uber's app to locate customers without also agreeing to pick up those passengers and charge the prices set by Uber—with or without driver input.

14. Federal Trade Commission, Comment Letter ("FTC Comment Letter") at 2, June 7, 2013, available at https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comments-district-columbia-taxicab-commission-concerning-proposed-rulemakings-passenger/130612dctaxicab.pdf.

15. Maureen K. Ohlhausen, Sharing Some Thoughts on the "Sharing Economy" (June 9, 2015), https://www.ftc.gov/system/files/documents/public_statements/671141/150609sharingeconomy.pdf.

16. Joshua D. Wright, "Has the D.C. cab commission forgotten who it serves?" WASHINGTON POST (Sept. 6, 2013), https://www.washingtonpost.com/opinions/has-the-dc-cab-commission-forgotten-who-it-serves/2013/09/06/cb-3d0c18-15a6-11e3-be6e-dc6ae8a5b3a8_story.html?utm_term=.4128057f1726.

17. *Philadelphia Taxi Ass'n, Inc. v. Uber Techs.*, No. CV 16-1207, 2016 WL 6525389 (E.D. Pa. Nov. 3, 2016).