



# Antitrust Treatment of Aftermarkets in the United States

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# Aftermarkets

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- Aftermarkets are prevalent, typically involving the sale of a product with follow-up sales of complementary consumables or service/maintenance
  - Simple products:
    - Razors and blades
    - Coffee makers and capsules
    - Printers and ink
  - More complex products:
    - Copiers/consumables, parts, and service
    - Software/updates, patches, service
    - Automobiles/parts, service
  - Other:
    - Flights/luggage fees
    - Hotels/spa, wifi, parking fees

# Aftermarkets

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- The basic issue in each instance is that the purchaser of the original product/service is “locked into” purchasing the aftermarket product/service from the same (or a designated) supplier.
- This is accomplished through:
  - Contract
  - Technical design
  - Practical cost of switching

# Legal Framework in United States

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- Leading case is *Eastman Kodak v. Image Technical Services* (Supreme Court 1992). It considered two theories:
  - Tying: Traditional analysis: Market power in tying market, two separate products, a requirement (contractual or technical) to purchase both products, and foreclosure of competition in tied product market.
    - (Tying not addressed in remainder of this presentation.)
  - Lock-in/exploitation: Market power that results from being locked-in to purchases as a result of original purchase decision. Market power in the primary market not necessary.

# Aftermarket Theory of *Kodak*

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- Principles of aftermarkets from *Kodak*
  - 1) If consumers are informed at outset that they must purchase products/services in the aftermarket from the same seller, consumers can consider “life-cycle” cost in purchasing decisions, and this will discipline ability to exploit aftermarket.
  - 2) However, there is room for concern if:
    - Change in policy regarding third-party sales in aftermarket or difficulty in assessing information before initial purchase; and
    - Difficult/costly to changing primary product after initial purchase.

## U.S. Cases Following *Kodak*

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- Few cases have followed *Kodak* to find antitrust liability for monopolizing aftermarkets. A sampling . . .
  - Rejected:
    - *DSM Desotech v. 3D Systems* (Fed. Cir. 2014) - Involved resin used in stereolithography machines (3-D printing), which was required to be purchased by machine maker; “Lock in” theory of *Kodak* applies only to customers who bought before policy change - most knew they would need to purchase from 3D Systems; resin prices easy to ascertain.

## U.S. Cases Following *Kodak*

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- Rejected:
  - *Alcatel USA v. DGI Technologies* (5th Cir. 1999) - Involved expansion cards for telephone network switches; customers were aware of costs of expansion cards when purchasing switches and relevant market not properly limited to expansion cards, given other ways to expand network capacity, limiting switch maker's market power.

## U.S. Cases Following *Kodak*

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- Rejected:
  - *Queen City Pizza v. Domino's Pizza* (3d Cir. 1997) - Involved franchise agreement that required purchase of approved pizza dough from Domino's (franchisor); franchisees by contract knew of restrictions on suppliers; relevant market not limited to Domino's pizza dough and included other doughs.



## U.S. Cases Following *Kodak*

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- Rejected:

- *Blizzard Entertainment v. Ceiling Fan Software* (D. Ct. 2013) - Involved third-party add-on “bot” to World of Warcraft online game; contractual/licensing limitation to only first party WoW add-ons meant any market power in aftermarket derived from contract and could be ascertained before purchase.
- *Clark Memorials v. SCI Alabama Funeral Services* (D. Ct. 2014) - Involved additional fee to install third-party gravestones at cemetery; no antitrust claim because consumers had been informed of policy before purchase of burial plot and fees were ascertainable.

## U.S. Cases Following *Kodak*

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- Accepted (?):
  - *Avaya v. Telecom Labs* (D. Ct. 2014) - Involved telephone equipment with after-sales service; jury found that equipment manufacturer had attempted to monopolize service aftermarket.
    - *Note*: jury verdict with less information about key facts; case currently on appeal.

# Lock-in Summary

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- Themes:
  - Information: If information about aftermarket prices is ascertainable, likely no aftermarket concern.
  - Contract: If there's a contractual limitation in advance, likely no aftermarket concern.
  - Change in policy: Change in policy must not be predictable to consumers, who are harmed by policy.

## A Closer Look at Lock-In Theory

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- General assumption of antitrust that consumers will consider available information, and thus account for cost of on-going service and/or consumables.
  - Compare typical focus on inter-brand competition, with less concern for intra-brand competition.
- Exceptions may exist when company tries to “exploit” consumers by taking advantage of lock-in through policy changes.
  - However, U.S. antitrust law does not typically address exploitative abuses (e.g., excessive pricing).

# A Closer Look at Lock-In Theory

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- Why do companies seek to limit third-party competition in aftermarkets?
  - Primary good and aftermarket good are typically complements.
  - Accordingly, selling both together can be efficiency enhancing:
    - Justifications similar with tying: improved control of quality; interoperability; reduce double marginalization; possibility of beneficial differential pricing (intensive/light users); others.
  - Compete on “systems” (razor + blade; software + updates/service) - may provide efficiencies and respond to consumer demand.

# The Role of Antitrust

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- What role for antitrust law?
  - “Exploitation” theory through change in policy
    - Can this work in practice, given reputational effect?
    - How often can a company “surprise” customers with unfavorable policy changes?
  - “Lack of information” theory
    - How likely in markets with sophisticated buyers?
    - Only some buyers need to process information fully to discipline primary market
  - Both theories constrained by extent of lock-in, limiting ability to charge supracompetitive prices.
  - Result in U.S. - almost no successful pure “aftermarket” antitrust cases; no FTC/DOJ challenges since *Kodak*.

# Alternative Approaches

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- If antitrust law is not appropriate to address concerns about exploitation of aftermarkets, are there other approaches?
  - Regulation - E.g., regulatory requirements regarding automobile parts/service designed to promote or ensure third party access.
    - Pros: Applies broadly to regulated market, not case by case.
    - Cons: Requires development of regulations and monitoring; may lead to inefficiencies.

# Alternative Approaches

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. . .other approaches?

- Consumer pressure - E.g., Keurig's K-cup coffee machine V.2 would not accept consumer refillable pod for use with third-party coffee. Consumer complaints, combined with low sales, led Keurig to revise limitation.
- Consumer protection laws - Are changed policies a possible unfair act or practice (FTC Act) in certain circumstances?
  - *Orkin* (FTC 1986) - "unfair" to increase fee in lifetime fixed fee termite protection contract.
  - Compare "drip pricing" - undisclosed fees that may be charged after initial purchase (hotels).





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Thank you!

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