In re Musical Instruments and Equipment Antitrust Litigation ("*Guitar Center*")

798 F.3d 1186 (9th Cir. 2015)

BEA, Circuit Judge:

Where a large musical-instrument retailer pressures individual guitar manufacturers to set the lowest prices at which the manufacturers will permit any retailer to advertise the manufacturers' products—and each manufacturer acquiesces—can we infer the manufacturers conspired among themselves to fix prices?

Plaintiffs ask us to answer this question in the affirmative. They claim it is plausible to infer a price-fixing conspiracy based only on allegations that certain guitar manufacturers each adopted similar advertising policies ("parallel conduct") under circumstances that suggest the manufacturers agreed among themselves to adopt those policies ("plus factors"). But plaintiffs' plus factors are no more consistent with an illegal agreement than with rational and competitive business strategies, independently adopted by firms acting within an interdependent market.

Plaintiffs' allegations of "merely parallel conduct that could just as well be independent action" are insufficient to state a claim under § 1 of the Sherman Act. *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 557 (2007). And because plaintiffs' plus factors add nothing, we affirm the judgment of the district court dismissing plaintiffs' § 1 claim.

I

Plaintiffs, a putative class, purchased guitars and guitar amplifiers from defendant Guitar Center, Inc. ("Guitar Center"), the largest retail seller of musical instruments in the United States. The guitars and amplifiers were manufactured by five major manufacturers, defendants Fender Music Instruments Corp., Gibson Guitar Corp., Yamaha Corp. of America, Hoshino U.S.A., Inc., and Kaman Music Corp. ("manufacturer defendants").

[P]laintiffs allege that between 2004 and 2009, Guitar Center and the manufacturer defendants—along with defendant trade association National Association of Music Merchants (NAMM)—conspired to implement and enforce minimum-advertised-price policies ("MAP policies") that fixed the minimum price at which any retailer could advertise the manufacturers' guitars and guitar amplifiers. According to plaintiffs, these MAP policies tended to raise retail prices and restrain competition. Plaintiffs allege that each manufacturer agreed with Guitar Center to adopt MAP policies and that the manufacturers agreed among themselves to adopt the MAP policies proposed by Guitar Center. Plaintiffs claim this collection of agreements violates § 1 of the Sherman Act.

Prior Federal Trade Commission Investigation and Settlement

In 2007, before plaintiffs filed any of the cases that now constitute this consolidated litigation, the Federal Trade Commission (FTC) initiated a nonpublic investigation into price fixing in the music-products industry. The FTC alleged that

> [b]etween 2005 and 2007, NAMM organized various meetings and programs at which competing retailers of musical instruments were permitted and encouraged to discuss strategies for implementing minimum advertised price

> policies, the restriction of retail price competition, and the need for higher retail prices.... At these NAMM-sponsored events, competitors discussed the adoption, implementation, and enforcement of minimum advertised price policies; the details and workings of such policies; appropriate and optimal retail prices and margins; and other competitively sensitive issues.

The FTC further alleged that the exchange of information among NAMM members (which include Guitar Center and the manufacturer defendants) "served no legitimate business purpose" and "had the purpose, tendency, and capacity to facilitate collusion and to restrain competition unreasonably." Neither Guitar Center nor the manufacturer defendants were parties to this FTC proceeding.

The FTC and NAMM resolved the dispute through a consent decree. In the consent decree, the FTC ordered NAMM to cease and desist from "urging, encouraging, advocating, suggesting, coordinating, participating in, or facilitating in any manner the exchange of information between or among Musical Product Manufacturers or Musical Product Dealers relating to ... Price Terms, margins, profits, or pricing policies, including but not limited to Minimum Advertised Price Policies." NAMM must also file periodic compliance reports and make a statement before each NAMM trade show informing members of the organization's and members' obligations under the antitrust laws. NAMM neither admitted nor denied the FTC's allegations, and the FTC did not levy any monetary fine.

Proceedings Below

After the FTC issued its consent decree, numerous plaintiffs filed complaints alleging that defendants agreed to fix the retail prices of musical instruments in violation of § 1 of the Sherman Act and state antitrust laws. The Judicial Panel on Multidistrict Litigation centralized twenty-eight of these cases in the Southern District of California.

Defendants moved to dismiss plaintiffs' first consolidated class-action complaint under Federal Rule of Civil Procedure 12(b)(6). Defendants argued that plaintiffs' allegations were insufficiently detailed to satisfy the requirements of specificity and plausibility that the Supreme Court had . . . outlined in *Twombly*.

The district court granted the motion to dismiss in part but permitted plaintiffs to amend their complaint. The district court found that plaintiffs failed to identify in their complaint "who is alleged to have conspired with whom, what exactly they agreed to, and how the alleged conspiracy was organized and carried out." Nor did plaintiffs "plead enough of the [MAP policies'] terms to show how they restrained competition." The district court gave plaintiffs a chance to remedy these problems by permitting some discovery. But because the district court agreed with defendants that "remarks at open panel discussions attended by many people at trade shows cannot reasonably constitute the terms of an illegal agreement in these circumstances," the court "limited discovery to who attended or participated in meetings alleged in the amended consolidated complaint and what was said or agreed to there."

Following this limited discovery, plaintiffs filed the operative complaint. Defendants again moved to dismiss the complaint for its failure to state a claim. The district court granted defendants' motion and dismissed plaintiffs' § 1 claim with prejudice for failure to satisfy the pleading standard set forth in *Twombly*. Plaintiffs timely appealed.

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III

A

The antitrust laws of the United States aim to protect consumers by maintaining competitive markets. To that end, § 1 of the Sherman Act prohibits agreements that unreasonably restrain trade by restricting production, raising prices, or otherwise manipulating markets to the detriment of consumers.

In analyzing the reasonableness of an agreement under § 1, the Supreme Court has distinguished between agreements made up and down a supply chain, such as between a manufacturer and a retailer ("vertical agreements"), and agreements made among competitors ("horizontal agreements").

The Supreme Court has recognized that certain horizontal agreements "always or almost always tend to restrict competition and decrease output." *Broadcast Music, Inc. v. CBS*, 441 U.S. 1, 19–20 (1979). . . .Vertical agreements, on the other hand, are analyzed under the rule of reason, whereby courts examine "the facts peculiar to the business, the history of the restraint, and the reasons why it was imposed," to determine the effect on competition in the relevant product market. *Nat'l Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679, 692 (1978). That analysis takes into account the fact that some vertical restraints may have procompetitive justifications that benefit consumers. *See Leegin Creative Leather Prods. v. PSKS, Inc.*, 551 U.S. 877, 889–92 (2007) (noting that vertical price restraints can have the procompetitive effect of increasing interbrand competition).

But the line between horizontal and vertical restraints can blur. One conspiracy can involve both direct competitors and actors up and down the supply chain, and hence consist of both horizontal and vertical agreements. Plaintiffs here allege one such hybrid form of conspiracy, sometimes called a "hub-and-spoke" conspiracy. . . . A traditional hub-and-spoke conspiracy has three elements: (1) a hub, such as a dominant purchaser; (2) spokes, such as competing manufacturers or distributors that enter into vertical agreements with the hub; and (3) the rim of the wheel, which consists of horizontal agreements among the spokes.

According to plaintiffs, Guitar Center (the hub) pressured each of the manufacturer defendants (the spokes) to adopt MAP policies, and the manufacturer defendants, in turn, each agreed among themselves to adopt the policies (the rim). NAMM acted to facilitate these illegal agreements by encouraging adoption of MAP policies—a role that may be illegal but lacks an obvious wheel analogue.

Section 1 prohibits agreements that unreasonably restrain trade, no matter the configuration they take or the labels we give them. A hub-and-spoke conspiracy is simply a collection of vertical and horizontal agreements. And once the conspiracy is broken into its constituent parts, the respective vertical and horizontal agreements can be analyzed either under the rule of reason or as violations per se.[3]

Here, the key agreements are those among the defendant manufacturers. . . . The question before us is whether plaintiffs have pleaded sufficient facts to provide a plausible basis from which we can infer the alleged agreements' existence.

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[3] Some courts have distinguished between "rimmed" and "rimless" hub-and-spoke conspiracies. . . . The extension of the wheel metaphor here may mislead: a rimless hub-and-spoke conspiracy is not a hub-and-spoke conspiracy at all . . .; it is a collection of purely vertical agreements. But such a conspiracy may yet unreasonably restrain trade. . . .

B

Because plaintiffs lack direct evidence of horizontal agreements among the manufacturers, they plead that the defendant manufacturers' parallel conduct in adopting MAP policies, in conjunction with several "plus factors," plausibly suggests the existence of horizontal agreements.

Under *Twombly*, parallel conduct, such as competitors adopting similar policies around the same time in response to similar market conditions, may constitute circumstantial evidence of anticompetitive behavior. But mere allegations of parallel conduct—even consciously parallel conduct—are insufficient to state a claim under § 1. Plaintiffs must plead "something more," "some further factual enhancement," a "further circumstance pointing toward a meeting of the minds" of the alleged conspirators.

In this way, *Twombly* takes into account the economic reality that mere parallel conduct is as consistent with agreement among competitors as it is with independent conduct in an interdependent market. . . .

In an interdependent market, companies base their actions in part on the anticipated reactions of their competitors. And because of this mutual awareness, two firms may arrive at identical decisions independently, as they are cognizant of—and reacting to—similar market pressures. In other words, competitors' behavior may be consciously parallel. Recognizing that parallel conduct may arise on account of independent business decisions rather than an illegal agreement, *Twombly* requires that when allegations of parallel conduct are set out to make a § 1 claim, plaintiffs must plead enough nonconclusory facts to place that parallel conduct "in a context that raises a suggestion of a preceding agreement." . . .

This court has distinguished permissible parallel conduct from impermissible conspiracy by looking for certain "plus factors." . . . Whereas parallel conduct is as consistent with independent action as with conspiracy, plus factors are economic actions and outcomes that are largely inconsistent with unilateral conduct but largely consistent with explicitly coordinated action. . .

Plaintiffs in their briefs and at oral argument identified the following six plus factors alleged in the operative complaint: (1) defendants shared a common motive to conspire; (2) the manufacturer defendants acted against their self-interest; (3) the manufacturer defendants simultaneously adopted substantially similar MAP policies; (4) the FTC's investigation and consent decree; (5) the defendants' participation in NAMM; and (6) retail prices for guitars and guitar amplifiers rose during the class period as the number of units sold fell. . .

Common Motive

Plaintiffs allege that the manufacturer defendants shared a similar motive to collude. But common motive does not suggest an agreement. Any firm that believes that it could increase profits by raising prices has a motive to reach an advance agreement with its competitors. Thus, alleging "common motive to conspire" simply restates that a market is interdependent (*i.e.*, that the profitability of a firm's decisions regarding pricing depends on competitors' reactions). Interdependence, however, does not entail collusion, as interdependent firms may engage in consciously parallel conduct through observation of their competitors' decisions, even absent an agreement. And allegations of parallel conduct—though recast as common motive—is insufficient to plead a § 1 violation.

Action Against Self–Interest

Plaintiffs allege that defendant manufacturers acted against self-interest by adopting MAP policies with Guitar Center. Again, plaintiffs fail to account for conscious parallelism and the pressures

of an interdependent market. An action that would seem against self-interest in a competitive market may just as well reflect market interdependence giving rise to conscious parallelism. For example, each firm in an interdependent market expects that a widely unfollowed price increase will be rescinded. But so long as prices can be easily readjusted without persistent negative consequences, one firm can risk being the first to raise prices, confident that if its price *is* followed, all firms will benefit. By that process ("follow the leader"), supracompetitive prices and other anticompetitive practices, once initiated, can spread through a market without any prior agreement.

More extreme action against self-interest, however, may suggest prior agreement—for example, where individual action would be so perilous in the absence of advance agreement that no reasonable firm would make the challenged move without such an agreement. Here, if no reasonable manufacturer would have entered into a MAP policy without assurances that all other manufacturers would enter into similar agreements, that would suggest collusion. But the complaint itself . . . provides ample independent business reasons why each of the manufacturers adopted and enforced MAP policies even absent an agreement among the defendant manufacturers.

Plaintiffs allege that each manufacturer was "pressured by Guitar Center" to adopt MAP policies that were advantageous to Guitar Center, and the complaint concedes that each manufacturer "responded to Guitar Center's pressure and coercion" by adopting MAP policies "in exchange for Guitar Center's agreement to purchase large volumes of the manufacturer's product stock." Manufacturers' decisions to heed similar demands made by a common, important customer do not suggest conspiracy or collusion. They support a different conclusion: self-interested independent parallel conduct in an interdependent market.

Simultaneous Adoption of MAP Policies

Plaintiffs allege that the manufacturer defendants simultaneously implemented and enforced MAP policies with similar terms. . . . But according to the complaint, the manufacturer defendants adopted the policies over a period of several years, not simultaneously. Allegations of such slow adoption of similar policies does not raise the specter of collusion. . . .

Even assuming that the progressive adoption of similar policies across an industry constitutes simultaneity, that fact does not reveal anything more than similar reaction to similar pressures within an interdependent market, or conscious parallelism. All of the manufacturer defendants were dealing with the same important customer, Guitar Center, which ostensibly exercised its considerable market power to demand similar terms from each manufacturer for its own benefit. The manufacturers' similar response to this market pressure is a hallmark of independent parallel conduct—not collusion.

The FTC's Investigation of NAMM

Plaintiffs argue that the FTC's investigation of NAMM suggests an agreement was made. The FTC alleged violations of § 5 of the Federal Trade Commission Act (FTC Act), which prohibits "unfair methods of competition." But unlike § 1 of the Sherman Act, a violation of § 5 of the FTC Act does not require allegation and proof of a contract, combination, or conspiracy. An organization may violate § 5 of the FTC Act without violating § 1 of the Sherman Act.[*] . . .

[*] [In practice, the FTC interpret the FTC Act's Section 5 in light of the established interpretations of the Sherman Act § 1. That is, the court's claim about Section 5 is incorrect.].

Defendants' Attendance of NAMM Meetings

Plaintiffs allege that Guitar Center advocated for the concerted adoption of anticompetitive MAP policies at NAMM meetings. But mere participation in trade-organization meetings where information is exchanged and strategies are advocated does not suggest an illegal agreement. . . .

Moreover, plaintiffs allege that the industry had encouraged the adoption of MAP policies as in each manufacturer's self-interest for years before the class period. Such an allegation does not suggest agreement; it provides a context for "merely parallel conduct that could just as well be independent action."

Rising Prices

Plaintiffs allege that the average retail price of guitars and guitar amplifiers rose during the class period as the total number of units sold fell. . . . Dissent at 1199–1200. We are not convinced [that this pattern is indicative of collusion].

First, plaintiffs do not allege that the average retail price of guitars and amplifiers manufactured by defendants rose during the class period. They allege an increase in the average retail price of all guitars and guitar amplifiers sold, including products outside the relevant product market, like low-cost imports. The same can be said of the alleged drop in sales.

But even if plaintiffs had alleged that retail prices of defendants' guitars and amplifiers rose in tandem as sales dropped, such a price increase is no more suggestive of collusion than it is of any other potential cause. Plaintiffs do not allege any facts connecting the purported price increase to an illegal agreement among competitors. And without such a connection, there is simply no basis from which we can infer an agreement. In this regard, parallel price increases, without more, are no different from other forms of parallel conduct. . . .

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The dissent urges that, "when analyzed together," plaintiffs' purported plus factors provide a context that plausibly suggests that "an illicit horizontal agreement was made between the manufacturer defendants." We disagree. Plaintiffs have indeed provided a context for the manufacturers' adoption of MAP policies, but not one that plausibly suggests they entered into illegal horizontal agreements. Instead, the complaint tells a different story, one in which Guitar Center used its substantial market power to pressure each manufacturer to adopt similar policies, and each manufacturer adopted those policies as in its own interest. Such conduct may be anticompetitive—and perhaps even violate the antitrust laws—but it does not suggest the manufacturers illegally agreed among themselves to restrain competition.

IV

Plaintiffs have failed to allege enough nonconclusory facts to support the plausible inference that any agreement among the manufacturers was made. For that reason, their § 1 claim must be dismissed.

AFFIRMED.

PREGERSON, Circuit Judge, dissenting.

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