UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

UNITED STATES OF AMERICA Plaintiff v. APPLE, INC., HACHETTE BOOK GROUP, INC., HARPERCOLLINS PUBLISHERS L.L.C., VERLAGSGRUPPE GEORG VON HOLTZBRINCK GMBH, HOLTZBRINCK PUBLISHERS, LLC d/b/a MACMILLAN, THE PENGUIN GROUP, A DIVISION OF PEARSON PLC, PENGUIN GROUP (USA), INC., and SIMON & SCHUSTER, INC., Defendants.	Civil Action No. 12-cv-2826

PENGUIN'S OBSERVATIONS WITH RESPECT TO THE GOVERNMENT'S RESPONSE TO PUBLIC COMMENTS AND MOTION FOR ENTRY OF FINAL JUDGMENT

The Court has allowed Penguin to file a brief submission to provide any "corrections" or "observations" about the Department of Justice's Tunney Act filings. (DE 94). Here it is: The Emperor has no clothes. The Government has made and critically relied upon the naked assertion that the advent of the agency method of selling eBooks (which the Government admits is intrinsically legal) (DE 81, at v) resulted in a steep increase in overall eBook prices, (*id.*, at 4-5), and its prohibition is necessary to reduce prices and allow competition to re-emerge (*id.* at 10-13). This claim of an agency-caused increase in eBook prices is thus the cornerstone of DOJ's argument that its attack on the agency model is in the public interest. (DE 81, at 11.)

Yet the Government has offered no empirical proof to clothe this claim. Rather it has represented to this Court and the public, pursuant to their Tunney Act obligations to disclose "determinative documents," that there are none, not even pricing studies. (DE 5, at 21) Neither were any government pricing studies or the like identified in the Response of Plaintiff United States to Public Comments on the Proposed Settlement ("DOJ Response"). On the other hand, numerous industry participants, with day-to-day knowledge of actual market pricing and deep experience in book selling, opine that overall eBook prices have decreased. Indeed, at least two commenters provided empirical studies demonstrating overall eBook price decreases.

Which is it? To be sure, prices for some titles of eBooks have gone up; but many others have decreased. One of the fundamental fallacies underlying the Government's proposed settlement (and its allegations in this litigation) is that eBook prices *were* $9.99 and then increased to $12.99 or some other definitive price point. (*See, e.g.*, DE 1, ¶ 7) This concept, however, is a myth—and, to get to the truth, one must systematically examine actual pricing, which the Government apparently has not. Or if the Government has done so, that analysis has not been shared with the Court or the public—calling into question the fairness and reliability of this Tunney Act procedure.

This Court's obligation, of course, is to determine if the settlements before it are in the public interest. As the vast majority of commenters have observed, the settlements the Government propose are far from typical and reach beyond its claims against the Settling Defendants to impose a regulatory scheme on industry participants who have nothing whatsoever to do with the claims in this litigation. We respectfully observe that a naked assumption about price effects under the agency model cannot be relied upon in determining whether such a remedy is in the public interest, especially when it is rebutted by fact-based, empirical proof.

I. Industry Experts Say eBook Prices Have Gone Down

Trying to put the best face on a bad situation, the DOJ Response announces that nearly 70 of the 868 public comments on the proposed decree "favored the suit and the settlement." (DE 81, at 2.) That calculates out to 92% of public comments that do not favor the proposed decree. DOJ brushes aside this avalanche of protesting comments as being self-interested. (*Id.*, at 2-3.)[1] The really important thing, however, is what these objecting commenters—people who know from first-hand knowledge what has happened in the industry—say factually about the issues. Scores of the commenters take issue with DOJ's price increase assertion. For example, Barnes & Noble squarely challenges, based upon an empirical pricing analysis, the validity of DOJ's claim of an eBook price increase. (ATC-97.) Another retailer commenter, Books-a Million, also insists that eBooks prices have gone down under the agency model, (ATC-261) as do the Harvard Bookstore (ATC-691), Diesel Book Store in California (ATC-16), Viewpoint Books in Indiana (ATC-20), Blue Bird Books in Colorado (ATC-187), Schuler Books & Music in Michigan (ATC-217), and numerous other bookstores where the public actually buy their books, including now, post-agency, eBooks. Likewise, a preeminent literary agency—representing some of the most

[1] Of course, we would assume that all those who took the time to comment are interested in one way or another. The 205 commenting book sellers can certainly be forgiven for wanting to preserve their right to choose the agency model—a right that will be denied under the decree, even though they did nothing wrong. And DOJ cannot be suggesting that the 8% minority who support the decree are all disinterested, objective neutral observers. In fact, DOJ says it considers just 2 of the 868 comments to be "neutral." (DE 81, at 2 n.3.)

well-known authors in America—has also done an empirical study that shows that there was no overall price increase for either non-bestselling or best selling eBook titles. (ATC-807.)

II. The Government Has No Credible Response

DOJ does not counter these challenges with any facts. Instead, it argues that, as the Government, it has access to "secret" sales data from other retailers—access that, for example, B&N lacks. (DE 81, at 29-30.) But DOJ never says what its secret data shows. All that DOJ points at to establish the alleged agency-produced eBook price increase is the statement of one "avid reader" who says that "on books she had purchased" prices had "gone up; very dramatically" since agency. (*Id.* at 30, n.19) (*quoting* ATC-0158.)

Perhaps more importantly, the Government has admitted to this Court and to the public, pursuant to its Tunney Act obligation to disclose "determinative documents," 15 U.S.C. §16(b), that there are no empirical economic studies it conducted to support its proposed decrees. (DE 5, at 21) The "thrust" of the disclosure requirement under the Tunney Act is "to bring into 'sunlight' the government's motives for entering a decree, thereby taking out of the 'twilight' the government's decision making processes with respect to antitrust settlements." *United States v. Bleznak*, 153 F.3d 16, 20 (quoting H.R. rep. No. 93-1463). As this Court has recognized, the legislative history of the Tunney Act specifically contemplated the disclosure of economic analyses prepared to evaluate the economic consequences of proposed consent decrees. *See United States v. Alex, Brown & Sons, Inc.*, 169 F.R.D. 532, 542 (S.D.N.Y. 1996) (noting that Senator Tunney expressly mentioned a "report analyzing the economic consequences" of a decree as falling squarely within the definition of "determinative documents"). Yet the Government affirmatively stated that none exist and has adduced no other credible evidence that it has nary a clue other than pure speculation (and the view of one "avid reader") about what was

going on with eBook pricing prior to the agency model or indeed what economic effects its proposed settlements will likely render.

The Court, the non-settling parties, and the public, are provided no reason, apart from the Government's own unsupported contentions (DE 81, at 4-6) for accepting the Government's summary conclusion that the Government's proposal for reshaping the nascent eBook marketplace will be better for competition or consumers than the other proposals that the it received and considered. Likewise, there is no explanation why or how the public interest will be served if the eBook industry returns to the conditions that prevailed when one monopoly seller dictated eBook prices through a strategy of loss leading certain titles for certain periods of time. There is no explanation of whether the Government has any empirical basis for predicting (or "hoping") the eBook market segment will "reset" and consumers, as a whole, will benefit. What can one call the Government's position other than a naked assertion?

III. eBook Pricing Was and Remains Complicated

Of course, as a non-settling Defendant in this case, Penguin now has access to all of the same "secret" sales data as does the Government. It is too complicated for purposes of this short submission to in any substantive way get into all of what the data show about pre- and post-agency eBook prices. What these data make clear, however, is that the Government is cherry-picking pricing throughout their Complaint and Tunney Act filings, i.e., focusing on the alleged Amazon $9.99 best-seller price because it suits their argument and ignoring the universe of all eBook prices (even though they allege an all "trade eBooks" relevant market). (DE 1, ¶ 99) Indeed, if Amazon persuaded DOJ that overall it was not losing money—as the DOJ lawyers and economists repeatedly told us—then DOJ knows that other prices of <u>something</u> were much higher than the alleged $9.99 new release price—to compensate for the obvious loss-leading.

If there is one point we think needs to be made clear, it is that there was no uniform $9.99 price point when Amazon was authorized to price each Publisher Defendants' eBook titles. We have looked at pre-agency, month-by-month pricing of Penguin new releases (*i.e.*, eBooks sold within 12 months of the release of the hardcover version) as priced and sold by Amazon during the one-year period prior to the advent of agency selling. What we found is that over 62% of the eBook titles for books with hard cover list prices over $20 (the typical range for bestsellers and other popular trade fiction) were priced by Amazon above $9.99, with many priced in the $14 to $15 dollar range. (*See* Exhibit A, at 1 (request to seal pending)) Indeed, for six of the twelve months pre-agency, the most common price point for such eBook titles was above $12.99. The price dispersion above $9.99 can be seen at page 2 (examining weighted average prices) and page 3 (actual monthly price points) of Exhibit A. We also note that prices for any specific title also changed, sometimes dramatically, over that title's life-cycle.

The pricing of eBooks may be a complex, but what is absolutely clear from that data is that the price of new release Penguin eBooks did not unvaryingly move from $9.99 to $12.99 post-agency. And, under the pricing ceilings regulating maximum retail eBook prices (contained in Penguin's agency contracts with Apple and Amazon), many of these eBook prices would have been less under the agency model. (Exhibit A, pp. 2-3) One would hope that the Government would have some justification for its proposed "solution" in light these facts. But none is offered.

IV. CONCLUSION

Penguin, in sum, respectfully observes that any pre-existing empirical analyses done by the Government to support its proposed settlements either do not exist or have been kept secret (thus tainting the Tunney Act process). Either way, it is hard for us to see how Government's naked pricing assertions can be relied upon to find its proposed consent decrees to be in the public interest.

Dated: August 15, 2012

Respectfully submitted,

/s/ Daniel Ferrel McInnis

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on August 15, 2012, I electronically filed the foregoing document using the CM/ECF system which will send notification of such filing to the e-mail addresses registered in the CM/ECF system, as denoted on the Electronic Mail Notice List.

Dated: August 15, 2012

_____/s/_____

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