United States District Court
For the Northern District of California

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SAN FRANCISCO DIVISION

Stacie Somers,

Plaintiff,

v.

Apple, Inc.,

Defendant.

/

NO. C 07-06507 JW

ORDER GRANTING DEFENDANT'S MOTION TO DISMISS WITH PREJUDICE

I. INTRODUCTION

Stacie Somers ("Plaintiff") brings this putative class action against Apple Computer, Inc. ("Defendant"), alleging violations of the Sherman Act, 15 U.S.C. §§ 2, *et seq.*, and California's Unfair Competition Law, Cal. Bus. & Prof. Code §§ 17200, *et seq*. Plaintiff alleges that Defendant has unlawfully updated its software to thwart programs that would have removed Digital Rights Management ("DRM") encryption from music files sold through Defendant's iTunes Music Store ("iTMS"), in violation of federal antitrust laws.

Presently before the Court is Defendant's Motion to Dismiss.[1] The Court conducted a hearing on June 20, 2011. Based on the papers submitted to date and oral argument, the Court GRANTS Defendant's Motion to Dismiss with prejudice.

[1] (Defendant's Motion to Dismiss Corrected Second Amended Complaint, hereafter, "Motion," Docket Item No. 118.)

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II. BACKGROUND

A. Factual Allegations

In a Second Amended Complaint filed on January 25, 2011,[2] Plaintiff alleges as follows:

On or about November 2005, Plaintiff purchased a 20GB iPod from Target, a third-party reseller of Defendant's products. (SAC ¶ 13.) Following the iPod purchase, Plaintiff purchased music from iTMS. (Id.) Defendant is a corporation organized under the laws of California whose principal place of business is in Cupertino, California. (Id. ¶ 14.)

In 2003, Defendant began to sell downloadable music with the launch of the iTMS. (SAC ¶ 2.) At that time, Defendant began restricting its iTunes program and the iTMS to work only with its own portable digital media player, the iPod, through the use of embedded proprietary DRM file encoding. (Id. ¶¶ 2, 34-35.) Thus, any consumer who wanted to play music purchased from the iTMS would be required to purchase an iPod, and iPod owners were required to purchase their music files from iTMS. (Id. ¶ 40.) Restrictions on DRM-embedded music files continue to this day, as owners of the files are still unable to play the files on other portable digital media players. (Id. ¶¶ 76-77.) In 2009, Defendant began selling DRM-free music, without restriction as to what type of player it could be played on. (Id. ¶ 4.) However, Defendant required its customers to pay a surcharge of 30 cents per song to convert prior music purchases to DRM-free files. (Id.)

Defendant maintained its monopoly power through "software updates" that prevented competitors from entering the market and threatening its monopolies. (SAC ¶¶ 50, 69.) For example, on July 26, 2004, Real Networks, a competing online digital music seller, announced that songs purchased through its store could be played on the iPod. (Id. ¶ 56.) In response, on July 29, 2004, Defendant issued a public statement to Real Networks: "We strongly caution Real and their customers that when we update our iPod software from time to time it is highly likely that Real's Harmony technology will cease to work with current

[2] (Corrected Second Amended Complaint, hereafter, "SAC," Docket Item No. 115.)

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and future iPods." (Id. ¶ 63.) Beginning in October 2004, Defendant updated its iPod software to prevent Real Networks' songs from being played on the iPod. (Id. ¶ 64.) In addition, Defendant continually issued software updates to prevent competitors from entering the market and threatening its monopolies, making it possible for Defendant to charge its customers the premium price of 30 cents per song for removal of DRM. (Id. ¶ 69.) These software updates prevented the use of programs that removed the DRM encryption from songs purchased from iTMS. (Id. ¶¶ 70-76.)

On the basis of the allegations outlined above, Plaintiff alleges four causes of action: (1) Monopolization (Injunctive Relief) in violation of Section 2 of the Sherman Antitrust Act, 15 U.S.C. §§ 2, *et seq.*; (2) Attempted Monopolization in violation of Section 2 of the Sherman Antitrust Act, 15 U.S.C. §§ 2, *et seq.*; (3) Monopolization (Damages) in violation of Section 2 of the Sherman Antitrust Act, 15 U.S.C. §§ 2, *et seq.*; and (4) Unfair Competition in violation of Cal. Bus. & Prof. Code §§ 17200, *et seq.*

B. Procedural History

On December 31, 2007, Plaintiff filed her Complaint in the present action on behalf of a class of indirect purchasers of Apple products ("Indirect Purchaser Action").[3] On February 15, 2008, the Court related the Indirect Purchaser Action to an action that made identical factual allegations and asserted the same causes of action against Defendant filed on behalf of direct purchasers of Apple products, The Apple iPod iTunes Antitrust Litigation, No. C 05-00037 JW ("Direct Purchaser Action"). (See Docket Item No. 12.) On February 23, 2009, Plaintiff in the Indirect Purchaser Action filed a Motion for Class Certification and Appointment of Co-Lead Class Counsel. (See Docket Item No. 39.) On July 17, 2009, the Court denied the Indirect Plaintiff's Motion for Class Certification as to the damages class under Fed. R. Civ. P. 23(b)(3), as Plaintiff failed to satisfy her burden to establish a reliable measure for damages in an action on behalf of

[3] (Complaint for Violations of Sherman Antitrust Act, Cartwright Act, California Unfair Competition Law, Consumer Legal Remedies Act and Monopolization of Business Practices, Docket Item No. 1.)

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indirect purchasers. (See Docket Item No. 80 at 12-13.) The Court declined to rule on class certification for the Rule 23(b)(2) class for injunctive relief. (Id.) On August 31, 2009, Indirect Purchaser Plaintiff again moved for class certification for the injunctive relief class, also seeking to expand her initial class definition to include "all purchasers of audio or video files from the iTMS since December 31, 2003." (See Docket Item No. 83 at 1.)

On October 3, 2009, the Court granted Direct Purchaser Action Defendant's Motion for Judgment on the Pleadings as to Plaintiffs' Rule of Reason Tying Claim under 15 U.S.C. § 1 and all related state claims in the Direct Purchaser Action on the ground that allegations of "a technological interrelationship between iTunes and iPods" failed to meet the threshold pleading requirement of a "coercive tying relationship."[4] In light of the dismissal of all tying claims, on December 21, 2009, the Court *sua sponte* decertified the Direct Purchaser Action Rule 23(b)(2) and 23(b)(3) classes based on allegations of violation of 15 U.S.C. § 2, and the Court granted Direct Purchaser Plaintiffs leave to amend their Complaint to include claims that did "not depend upon allegations of tying as the anticompetitive conduct upon which they base their monopoly claims." Further, the Court invited the Direct Purchaser Plaintiffs to merge the injunctive relief requested in the Indirect Purchaser Action into their prayer for relief "because they derive from the same alleged anticompetitive conduct by Apple."[5] Also in its December 21, 2009 Order, the Court ordered Indirect Purchaser Plaintiff to show cause why the Indirect Purchaser Action should not be dismissed "since the basis for a separate action, namely, indirect purchasers of iPods, is no longer viable in light of the Court's denial of certification of the damages class." (Id. at 11.) Further, once the Direct Purchaser Plaintiffs amended their pleadings to include the injunctive relief sought by the

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[4] (Order Granting Defendant's Motion for Judgment on the Pleadings as to the First Cause of Action for Violations of Section 1 of the Sherman Act and the Fifth Cause of Action for Violations of the Cartwright Act at 10, hereafter, "October 30 Order," C 05-0037-JW, Docket Item No. 274.)

[5] (Order Decertifying Classes Without Prejudice to Being Renewed; Inviting Further Motions at 2-3, 11, hereafter, "December 21, 2009 Order," C 05-0037-JW, Docket Item No. 303.)

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Indirect Purchaser Action, it appeared to the Court that the Indirect Purchaser Action would no longer be necessary. (Id. at 11-12.)

On February 1, 2010, the Indirect Purchaser Plaintiff filed her Response to the Court's Order to Show Cause. (See Docket Item No. 91.) On June 29, 2010, following a review of the Direct Purchaser Plaintiffs' Amended Consolidated Complaint, the Court held that the remedies and class represented by the Indirect Purchaser Action were distinct from the Direct Purchaser Action.[6] For instance, the Court found that the Direct Purchaser Action did not purport to represent purchasers of digital files from the iTMS and the Indirect Purchaser Action sought solely injunctive relief. (Id. at 16.) Despite the Court's December 21, 2009 Order inviting the Direct Purchaser Action to amend their pleadings to incorporate the injunctive relief sought by the Indirect Purchaser Action, the Direct Purchaser Plaintiffs declined to so amend. (Id.) Thus, as the two Actions sought to represent two distinct classes of Apple consumers and did not pray for the same remedies, the Court found the Indirect Purchaser Action "not redundant or unnecessary at this time." (Id.) In light of the Court's allowing the Indirect Purchaser Action the right to proceed, the Court further granted Indirect Purchaser Plaintiff leave to "file an Amended Complaint that does not depend on allegations of tying as the anticompetitive conduct upon which [she] basis [her] monopolization claims." (Id.)

Additionally, in the June 29 Order, the Court denied Defendant's Motion to Dismiss the Direct Purchaser Plaintiffs' Sherman Act Section 2 claim, as the Direct Purchaser Plaintiffs had alleged sufficient facts to state a claim for monopolization. (June 29 Order at 5-7.) Specifically, the Court held that the Direct Purchaser Plaintiffs satisfied the second element required to state a claim for monopolization by alleging that "Defendant used software updates to maintain its monopolies in both the digital media and portable media player markets by preventing competing online music stores from offering customers digital files that could be played on the iPod, and by preventing competing music players from being able to play digital files from the [iTMS]." (Id.)

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[6] (Order Granting in Part and Denying in Part Defendant's Motion to Dismiss; Denying as Premature Defendant's Motion for Summary Judgment; Granting Indirect Purchaser Plaintiff Leave to File an Amended Complaint at 15-16, hereafter, "June 29 Order," Docket Item No. 99.)

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On July 9, 2010, Indirect Purchaser Plaintiff filed her First Amended Complaint. On December 21, 2010, the Court granted Defendant's Motion to Dismiss Plaintiff's First Amended Complaint. (hereafter, "December 21, 2010 Order," Docket Item No. 113.) The Court dismissed Plaintiff's claims for compensatory damages for diminution of iPod value on the ground that Plaintiff's claims were asserted as an indirect purchaser, which meant that Plaintiff could not recover damages under federal antitrust law. (Id. at 8-9.) Further, the Court dismissed Plaintiff's claims for antitrust violations based on the theory that Defendant's charge of 30 cents per song for DRM-free music constituted anticompetitive conduct, as Plaintiff had failed to sufficiently plead that the 30-cent charge for DRM-free music resulted from anticompetitive software updates. (Id. at 9-11.) Finally, the Court dismissed Plaintiff's claims for antitrust violations based on the theory that Defendant charged supracompetitive prices for music purchased from iTMS, as Plaintiff did not allege facts showing that Defendant's iTMS pricing was supracompetitive, and Plaintiff also alleged in a contradictory fashion that Defendant's pricing remained at the same price per unit since its entry into the market.[7] (Id. at 11-12.) The Court granted Plaintiff leave to amend her Complaint, but ordered that Plaintiff "shall allege facts sufficient to support standing to bring her [antitrust claims] and shall not reallege any theories that the Court has previously found to be [anticompetitive]." (Id. at 13.)

Presently before the Court is Defendant's Motion to Dismiss Plaintiff's Second Amended Complaint.

III. STANDARDS

Pursuant to Federal Rule of Civil Procedure 12(b)(6), a complaint may be dismissed against a defendant for failure to state a claim upon which relief may be granted against that defendant. Dismissal may be based on either the lack of a cognizable legal theory or the absence of sufficient facts alleged under a cognizable legal theory. Balistreri v. Pacifica Police Dep't, 901 F.2d 696, 699

[7] In addition, the Court dismissed Plaintiff's state law claims, because the Court found that they lacked "sufficient allegations of unfair and unlawful conduct to state a claim" in light of the Court's dismissal of Plaintiff's federal antitrust claims. (Id. at 13.)

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(9th Cir. 1990); Robertson v. Dean Witter Reynolds, Inc., 749 F.2d 530, 533-34 (9th Cir. 1984). For purposes of evaluating a motion to dismiss, the court "must presume all factual allegations of the complaint to be true and draw all reasonable inferences in favor of the nonmoving party." Usher v. City of Los Angeles, 828 F.2d 556, 561 (9th Cir. 1987). Any existing ambiguities must be resolved in favor of the pleading. Walling v. Beverly Enters., 476 F.2d 393, 396 (9th Cir. 1973).

However, mere conclusions couched in factual allegations are not sufficient to state a cause of action. Papasan v. Allain, 478 U.S. 265, 286 (1986); see also McGlinchy v. Shell Chem. Co., 845 F.2d 802, 810 (9th Cir. 1988). The complaint must plead "enough facts to state a claim for relief that is plausible on its face." Bell Atl. Corp. v. Twombly, 550 U.S. 544, 570 (2007). A claim is plausible on its face "when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." Ashcroft v. Iqbal, 129 S. Ct. 1937, 1949 (2009). Thus, "for a complaint to survive a motion to dismiss, the non-conclusory 'factual content,' and reasonable inferences from that content, must be plausibly suggestive of a claim entitling the plaintiff to relief." Moss v. U.S. Secret Serv., 572 F.3d 962, 969 (9th Cir. 2009). Courts may dismiss a case without leave to amend if the plaintiff is unable to cure the defect by amendment. Lopez v. Smith, 203 F.3d 1122, 1129 (9th Cir. 2000).

IV. DISCUSSION

Defendant moves to dismiss Plaintiff's Second Amended Complaint on the grounds that Plaintiff failed to cure the defects in her First Amended Complaint, as follows: (1) Plaintiff again fails to allege sufficient facts to show that Defendant charged supracompetitive prices for music sold through iTMS, and the claim is still undermined by Plaintiff's own allegations; and (2) Plaintiff's claim relating to Defendant's charge for DRM-free versions of previously purchased music files still relies on the assertion that Defendant acted wrongfully in adopting DRM, in contravention of the Court's prior Orders holding that the adoption and maintenance of DRM does not constitute anticompetitive conduct. (Motion at 4-11.) Plaintiff responds that dismissal is improper, because: (1) the Complaint contains sufficient allegations to show that Defendant charged supracompetitive

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prices; and (2) but for Defendant's introduction of unlawful software updates, Defendant would not be able to charge for "replacement DRM-free files."[8] The Court addresses each ground in turn.

A. iTMS Supracompetitive Price Theory

Defendant moves to dismiss Plaintiff's claims for antitrust violation on the theory of iTMS supracompetitive pricing on the grounds that: (1) Plaintiff alleges no facts showing that Defendant's pricing was supracompetitive; and (2) Plaintiff does not allege that Defendant's prices varied during the relevant period in any way that supports her claim. (Motion at 4-9.) Plaintiff responds that: (1) Defendant's software updates "deliberately thwarted" programs that removed DRM protection from songs purchased from iTMS, and those programs would have made the market for digital music more competitive, which would have inevitably resulted in lower prices; and (2) Defendant charged a "premium price" of $1.29 per song (rather than 99 cents per song) for DRM-free songs from EMI's catalog between April 2007 and January 2008. (Opp'n at 11-14.)

Here, in support of the iTMS supracompetitive pricing claim, Plaintiff alleges as follows:

> Defendant introduced various "software updates" whose clear purpose and intent was to maintain and further entrench Defendant's monopoly power in the audio download market. (SAC ¶ 50.) Defendant used these software updates to shut out competitors and cut off their access to the marketplace. (Id.) In October 2004, Defendant updated its iPod and iTunes software to prevent songs downloaded from Real Networks' music store from being played on iPods, thereby thwarting Real Networks' effort to compete with Defendant in selling music that was compatible with the iPod and enabling Defendant to artificially maintain its monopoly power in the audio download market. (Id. ¶¶ 64-66.) Real Networks made clear its intention to offer competition in the market for Audio Downloads that could be played on iPods, pricing its Audio Downloads at a significant discount to the prices charged by Defendant. (Id. ¶ 133.) Also, starting in October 2005, Defendant released a series of software updates designed to thwart programs such as JHymn and QTFairUse, which removed DRM encryption from songs purchased on iTMS. (Id. ¶¶ 69-77.) These programs attempted to allow consumers to enjoy the fair use of their purchases, and by thwarting them, Defendant was attempting to entrench and profit from its DRM. (Id.)

These allegations offer two types of support for Plaintiff's iTMS supracompetitive pricing claim: (1) the allegation that Defendant's competitor Real Networks offered music downloads at a lower price than Defendant; and (2) the allegation that Defendant maintained its monopoly over the music download market by issuing software updates to "thwart" programs that removed the DRM

[8] (Opposition to Defendant's Motion to Dismiss Corrected Second Amended Complaint at 6-15, hereafter, "Opp'n," Docket Item No. 119.)

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encryption from songs purchased on iTMS. As to the first of these, the Court finds that it is identical to the allegation that "competitor Real Networks' pricing for audio downloads was priced lower than Defendant's audio downloads," which the Court has already found insufficient to support the allegation that Apple's iTMS pricing was supracompetitive. (See December 21, 2010 Order at 12.) As to the second of these, the Court finds that it relies on the presumption that Defendant's maintenance of its DRM encryption constituted an antitrust violation; however, the Court has repeatedly found that this presumption is insufficient to support Plaintiff's antitrust claims. (See December 21, 2009 Order at 2; December 21, 2010 Order at 11.)

In an effort to save her Complaint, Plaintiff raises for the first time a new theory to support her antitrust claim. Plaintiff contends that Defendant charged $1.29 per song for DRM-free music from EMI between April 2007 and January 2008, when a competitor to Defendant began selling DRM-free music for no more than 99 cents per song.[9] (Opp'n at 14.) Plaintiff further contends that Defendant responded to the competitor's pricing by selling its own DRM-free music for 99 cents per song. (Id.) However, on Plaintiffs' own allegations, Defendant has been selling music downloads for 99 cents per song since the time Defendant began operating the iTMS in 2003. (SAC ¶¶ 34-35, 57.) Thus, the fact that Defendant began charging 99 cents for DRM-free music from the EMI catalog after January 2008 cannot constitute support for the claim that Defendant was supracompetitively pricing its iTMS sales earlier.

Accordingly, the Court GRANTS Defendant's Motion to Dismiss Plaintiff's federal antitrust claims based on iTMS supracompetitive pricing with prejudice.

B. DRM-Free Music Charge

Defendant moves to dismiss Plaintiff's claim seeking injunctive relief of free DRM-free music files for antitrust violations, on the ground that the claim simply reiterates Plaintiff's earlier theory, previously held insufficient by the Court, that Defendant acted wrongfully in adopting DRM.

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[9] Although Plaintiff does not plead this theory in her Second Amended Complaint, but raises it in her Opposition, the Court addresses it to demonstrate that even if the Court were to give Plaintiff leave to amend, yet again, these factual allegations would be insufficient to state an antitrust claim against Defendant.

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(Motion at 9-11.) Plaintiff responds that the Complaint contains new allegations that Defendant introduced software updates to intentionally thwart programs that removed DRM from music files sold by Defendant, which adversely affected competition because DRM-removing programs could help Defendant's competitors sell products that could compete with Defendant's products. (Opp'n at 9-11.)

Here, in support of the claim for DRM-free music, Plaintiff alleges as follows:

> Defendant continually issued "software updates" to prevent competitors from entering the market and threatening its monopolies, making it possible for Defendant to charge its customers a premium price for removal of DRM. (SAC ¶ 69.) These software updates thwarted such programs as JHymn, QTFairUse, PlayFair, and Requiem, which removed the DRM from music files purchased from iTMS. (Id. ¶¶ 70-76.) Those programs provided a workaround to Defendant's DRM technology, and industry analysts believed that they could help other companies sell iTunes compatible products that could start to scratch away at Defendant's dominance in the iPod market. (Id. ¶ 74.)

The Court finds that Plaintiffs' allegations in support of its claim for DRM-free music depend on the claim that Defendant's maintenance of its DRM, through software updates that "thwarted" programs which removed the DRM, was unlawful. However, as discussed previously, the Court has repeatedly found that an allegation of "mere maintenance of DRM" is insufficient to support Plaintiff's antitrust claims.

Accordingly, the Court GRANTS Defendant's Motion to Dismiss Plaintiff's federal antitrust claims for DRM-free music with prejudice.[10]

Because of the Court's disposition of Plaintiff's federal antitrust claims, which serve as the basis for Plaintiff's state law claims, the Court finds that Plaintiff's state law claims lack sufficient allegations of unfair and unlawful conduct to state a claim. Accordingly, the Court GRANTS Defendant's Motion to Dismiss Plaintiff's state law claims with prejudice.

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[10] Here, dismissal with prejudice is proper because, unlike the Direct Purchaser Action, which involves purchasers of iPods and the contention that various iterations of iTunes have changed the internal workings of the iPod, thereby affecting those purchasers, this Indirect Purchaser Action only involves purchasers of music downloaded from the iTMS. Thus, even if Plaintiff were to be granted leave, yet again, to amend her Complaint, she would not be able to state a claim under the same theory of anticompetitive conduct presented in the Direct Purchaser Action.

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V. CONCLUSION

The Court GRANTS Defendant's Motion to Dismiss Plaintiff's Second Amended Complaint with prejudice.

Dated: June 27, 2011

JAMES WARE
United States District Chief Judge

THIS IS TO CERTIFY THAT COPIES OF THIS ORDER HAVE BEEN DELIVERED TO:

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Dated: June 27, 2011

Richard W. Wieking, Clerk

By: /s/ JW Chambers
Susan Imbriani
Courtroom Deputy

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