



California May Be Trying to Evade the Consumer Welfare Standard in Its Antitrust Lawsuit against Amazon

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Attorney General Rob Bonta of California has filed an antitrust lawsuit against Amazon.¹ The central allegation in the complaint is that whenever third-party sellers want to offer their products through Amazon Marketplace, Amazon forces the sellers to agree its price parity policy, which requires that any products sold through Amazon Marketplace not be offered elsewhere online at lower prices. At first glance, it appears that Amazon is trying to make sure shoppers on its website get the lowest prices. However, the California complaint argues that rather than leading to lower prices, the price parity policy actually leads to higher online prices because third-party sellers cannot offer their products on other online retail websites, including their own websites, at lower prices than they charge for sales through Amazon Marketplace.

This isn't the first time Amazon has faced an American antitrust lawsuit. The District of Columbia attorney general filed a similar complaint against Amazon in 2021.² The District of Columbia complaint was dismissed in 2022 and is currently under appeal. The Federal Trade Commission is also investigating Amazon and presumably considering bringing a similar antitrust case.³

Compared with the District of Columbia lawsuit, the California action has a greater chance of success, but this is due to particularities of California antitrust law. Most antitrust lawsuits are brought under federal antitrust laws, which in this case would require that the California attorney general show actual harm to Amazon shoppers. But California's antitrust and unfair competition law is less reliant on the consumer welfare standard, so evidence of harm is less important. This difference in antitrust standards is likely a key reason why the California attorney general brought the case in a California state court under state law. If the California attorney general achieves a litigation win over Amazon that is not based on the consumer welfare standard, that win will

undermine the principle that antitrust decisions should be based on economic analysis rather than political considerations.

The California complaint offers plausible theories of how buyers using the Amazon site might be hurt by Amazon's price parity requirement. The complaint alleges that Amazon may discourage competition from other retail sites and that Amazon may be trying to raise fees it charges sellers who use Amazon Marketplace. But there is also evidence that Amazon's policies benefit consumers and that the relief California is seeking will help sellers who use Amazon Marketplace while possibly making things worse for Amazon shoppers.

Bringing the case under the California laws gives the state attorney general an easier path to get around the federal consumer welfare standard, avoiding having to show harm to customers of the Amazon website, and instead relying on complaints from sellers who want Amazon to offer them more favorable terms that won't necessarily help consumers.

The California case may lead to Amazon being found liable for its price parity policy regardless of whether it benefits those who purchase goods on Amazon. If California ultimately succeeds, one can expect more weaponizing of antitrust enforcement to target companies for their size rather than for any harm to consumers. Those who are alarmed with Amazon's size and success may cheer this outcome, but such a win by the California attorney general would not be an outcome worth celebrating for those who care about the benefits to everyday consumers.

WHY THE CONSUMER WELFARE STANDARD MATTERS

Before the US Supreme Court embraced the consumer welfare standard in the late 1970s, judicial antitrust rulings were inconsistent and often based on a poor understanding of economics. Not only did antitrust caselaw fail to provide any meaningful guidance that could promote consistent and predictable enforcement, but the inconsistency created a void, which was eventually filled by activist antitrust enforcers substituting their judgment for those of the market.

In 1966, Justice Potter Stewart showed his frustration with the lack of consistent standards in antitrust enforcement when he famously wrote in dissent in a merger case involving two local supermarket chains: "The sole consistency that I can find is that, in litigation under § 7, the Government always wins."⁴ Justice Stewart's point, made shortly before the consumer welfare standard was adopted, is that in the absence of a clear and principled standard, antitrust violations may be whatever the government enforcers want them to be. When antitrust enforcers are not bound by the consumer welfare standard, they can use the antitrust laws to favor some businesses over others.⁵ Or they can promote unrelated public policies such as favoring labor interests,⁶ combatting racial discrimination,⁷ combatting climate change,⁸ and even punishing political opponents.

The Supreme Court recognized the concept of the consumer welfare standard in a series of cases in the late 1970s. In 1977, the Supreme Court held that business conduct raising antitrust concerns must be evaluated on the basis of “demonstrable economic effect.”⁹ In the same year, the Supreme Court stated firmly that the antitrust laws were enacted for “the protection of competition, not competitors.”¹⁰ Two years later, the Supreme Court explicitly described the Sherman Antitrust Act as a “consumer welfare prescription.”¹¹ The consumer welfare standard quickly became relatively uncontroversial in antitrust law, at least until recently.¹²

The consumer welfare standard provides an important check on enforcers trying to pick economic winners and losers. The consumer welfare standard focuses the antitrust review on one simple question: does the conduct make consumers better or worse off? Abandoning the consumer welfare standard opens the door to a return to the inconsistent and sometimes unprincipled antitrust enforcement of the past.

SUMMARY OF THE ALLEGATIONS IN THE CALIFORNIA COMPLAINT AGAINST AMAZON

Sales on the Amazon website fall into two broad categories: those made by Amazon acting as a retailer on its own platform, which are not at issue in the California lawsuit, and those made by third-party sellers who contract with Amazon to make their products available directly to shoppers through Amazon Marketplace, which is where the California complaint asserts that the antitrust harm is occurring. According to the California complaint, over half of the sales on the Amazon website are third-party sales through Amazon Marketplace.

For access to Amazon Marketplace, third-party sellers pay Amazon referral fees, which typically are a percentage or minimum dollar amount per unit sold. They also pay Amazon fees for shipping, fulfillment, stocking, storage, advertising, and other services. Some third-party retailers participate in Amazon’s Fulfilled by Amazon (FBA) program, which means that Amazon holds the inventory of the retailer in an Amazon fulfillment center and packs and ships the order. These FBA sales may qualify for Amazon Prime designation. Third-party retailers who do not participate in the FBA program do not qualify for Amazon Prime designation.

The complaint alleges that Amazon required third-party sellers to enter into various types of contractual agreements in order to sell their products through Amazon Marketplace. These agreements contained a price parity requirement, which prohibits third-party sellers from offering their products on other online retail websites at lower prices than they charge through Amazon Marketplace.

For example, if a seller offers a product through Amazon Marketplace for \$10, that seller is free to sell on its own website or another website such as Walmart.com or eBay, so long as the seller does not charge less than \$10 on the other websites. This practice guarantees consumers that they can find the lowest price on Amazon.

According to the complaint, if a seller fails to comply with the price parity policy, Amazon may have the seller's products demoted in the search algorithm on the Amazon website so that the products are less likely to be noticed by shoppers. Amazon may also exclude the seller's products from Amazon's Buy Box feature, which suggests items for customers to add their carts at checkout. The complaint also alleges that Amazon requires that some sellers refund the price difference if their product is offered for less on a competing website.

AMAZON'S PRICE PARITY POLICY APPEARS TO FAVOR CONSUMERS

Amazon's price parity policy is a guarantee to consumers that they can find the lowest price on Amazon. To most shoppers, that will appear to be a benefit of buying on the Amazon site—they can know that they are getting the best price determined by competition among sellers who use Amazon Marketplace. Yet the California complaint turns that guarantee on its head, claiming that the price parity policy is really a minimum price for sales on non-Amazon websites that hurts shoppers by preventing them from buying at a lower price from another online site.

Which story is correct? Does Amazon's policy lead to lower or higher prices for online shoppers?

Several key facts support the version that Amazon's policy does more to keep prices low for shoppers. Amazon can claim that it is watching out for its customers by insisting that they get the lowest available price from third-party retailers when they shop on the Amazon website. Amazon also does not impose any specific prices on sellers. Sellers are free to set any price they want for any product, so long as they don't offer the same product at a lower price on another website. Moreover, California is not alleging that Amazon requires sellers to maintain price parity as a condition for doing business. Instead, Amazon is offering incentives for sellers to maintain price parity, but California does not appear to be alleging that Amazon will exclude any seller that does not comply. In addition, Amazon has a long history of and reputation for pushing for the lowest possible prices.

Thus, the economic analysis of what Amazon is doing is complicated, and it is not at all clear that the economic impact can be assessed convincingly. Perhaps the California attorney general can develop evidence to support the theory that preventing the Amazon policy keeps prices higher on other websites. But at first glance, it seems more likely that Amazon's price parity policy leads to lower prices. Under the consumer welfare standard, the California attorney general has a burden to put forward a convincing model. Thus, the challenge for the California attorney general is to find evidence to prove that Amazon's pricing parity requirement hurts shoppers enough to overcome the obvious benefit to shoppers.

DOES THE PRICE PARITY POLICY LEAD TO HIGHER FEES BY AMAZON?

According to the California complaint, a major source of harm to Amazon shoppers from the price parity policy is that it gives Amazon an incentive to raise fees. The complaint claims, “absent Amazon’s anticompetitive agreements, the market would be expected to reflect lower prices at competing online stores, given the inflated fees Amazon charges to merchants to sell on or through its platform.”¹³

The California complaint appears to be starting from the premise that Amazon charges fees that are proportional to the amount sold, so it follows that a third-party seller will want to charge a higher price on the Amazon website than on its own website, where the seller does not have to pay fees to Amazon. But that framing of the economic analysis only tells part of the story. Sellers have demonstrated that it is important for them to be on the Amazon website, so they must be receiving meaningful benefits from placing their products there. Amazon also incurs some costs from making other sellers’ products available on its website, so merely charging fees for these product placements does not by itself make Amazon’s price parity policy anticompetitive.

It is possible that the California complaint identified harm to consumers because Amazon’s fees are inflated to anticompetitive levels that are reflected in higher prices for consumers. Still, there are good reasons to be skeptical. Many companies use similar price parity contract requirements, which are usually considered procompetitive and which are therefore evaluated for their economic impact under the consumer welfare standard.¹⁴

If Amazon were using its price parity policy to hide a scheme to inflate the fees it charges third-party sellers, one would expect that practice also to inflate the profits of competing online marketplaces by preventing them from being undercut by Amazon and other online sites. Then these other online sites could further benefit by raising their own fees and reinvesting the higher profits to improve their sites and increase capacity so that they can better compete with Amazon. Or if the competing sites were to decide not to raise fees, the profits for third-party sellers would increase, and these sellers would prefer to do more business with other sites and less business with Amazon. If Amazon were using its price parity policy simply to hide its higher fees, it would risk boosting competing websites. Although it is plausible that the price parity policy leads to Amazon’s taking advantage by raising fees, the claim is questionable.

DOES PAYING LESS ON OTHER WEBSITES ACTUALLY HELP CONSUMERS?

A key claim in the California complaint is that the price parity policy causes anticompetitive harm by preventing third-party sellers from charging a lower price on their own websites. According to the complaint, “Absent Amazon’s anticompetitive agreements, the market would be expected to reflect lower prices at competing online stores, given the inflated fees Amazon charges to merchants to sell on or through its platform.”¹⁵ The complaint quotes a third-party seller who states,

“I think what would be best for consumers . . . would be for us to have our products on our website for less. Simultaneously, our products on Amazon would be higher but at the same profit per unit, and then customers could essentially choose.”¹⁶

What this third-party seller is describing is a free rider arrangement. The seller would like to see its customers go to the Amazon website to gather information about a product and then turn to the seller’s website to buy it for less.

Being a free rider is a good deal for third-party sellers: Amazon incurs the costs of providing information about a seller’s products on the Amazon site, and after shoppers learn about a product, they can turn to the seller’s website for a lower price. That way, a free riding seller can potentially get more sales for itself and save on advertising and promotion while Amazon in effect subsidizes these sales through its promotion of the products.

But is such free riding good for buyers? Most of the time it isn’t. The company supporting the free rider usually can find a way to get around having to subsidize someone taking advantage of it like this.

If Amazon is forced by the California courts to end its pricing parity policy, then one of its options is to stop carrying products from third-party sellers whenever it is concerned that the sellers will price their products lower on their own websites. A key reason why some third-party sellers want to free ride is because of Amazon’s success creating an online ecosystem that other online marketplaces have not been able to replicate. If Amazon responds by cutting off third-party sales, then these sellers will lose access to the successful Amazon ecosystem, which they are unlikely to be able to replicate because of the massive investment needed to build an alternative system and the uncertainty of a return. This action would leave everyone worse off, because a third-party seller would simply sell through its own website, as if Amazon had never existed in the first place. Shoppers on Amazon will have access to fewer products, will be less likely to discover certain products, and instead may find a competitor.

Amazon may have other ways of responding to free riding. Amazon probably could price services using two-part pricing: a fixed price for product promotion and a price per unit sold for services that vary with quantity such as order fulfillment. In this case, if the value of each service were at least equal to the price charged for it, there wouldn’t be an incentive to free ride by offering lower prices on other sites. That Amazon does not already structure its charges in this way may suggest that something else is going on—something anticompetitive. But merely showing that Amazon did not narrowly tailor its fee structure to combat free riding is not enough to show anticompetitive harm, and the burden is still on the California attorney general to show such harm.

Being the lowest-price seller most likely brings at least some customers to the Amazon website, which benefits third-party sellers. Those customers could be lost if Amazon were forced to end

its price parity policy. To the extent that attracting customers through Amazon Marketplace is important to third-party sellers, they would likely ensure price parity voluntarily in order to get any additional sales that occur because consumers are confident they are getting the best price. Most likely, not all sellers would do this, and some would try to free ride if they can. But if that is true, California cannot simply focus on any harms to sellers who don't like the price parity policy; the state must take into account the perceived benefits to those sellers who believe they benefit from Amazon's assurance that the prices are lowest on Amazon Marketplace.

DO THIRD-PARTY SELLERS WITHHOLD PRODUCTS FROM AMAZON BECAUSE OF THE PRICE PARITY POLICY?

The California complaint also asserts that some sellers withhold some of their products from Amazon because of the price parity requirements, thereby leaving Amazon shoppers with fewer choices. This could be a case of consumer harm. However, this claim is less well developed than other claims in the California complaint. The state offers little empirical evidence that harm is occurring or that Amazon shoppers lack easily accessible alternatives.

As with the other allegations in the California complaint, it may be possible for the California attorney general to show harm of this nature. But there are also good reasons to believe that the alleged harm isn't happening or that there are other benefits to consumers that are not described in the complaint. Under the consumer welfare standard, the California attorney general has to show that not only do the harms it alleges actually occur, but also that any benefits of the policy to Amazon shoppers add up to less than the cost of the alleged harms.

STATE ANTITRUST LAW IN CALIFORNIA VS. FEDERAL ANTITRUST LAW

The most notable difference between the California complaint against Amazon and the recently dismissed complaint by the attorney general for the District of Columbia is that California's complaint alleges violations of California's state antitrust laws, which differ from the federal laws. The district's complaint alleged violation of the district's antitrust laws, which mirror the federal antitrust laws. On March 18, 2022, the judge dismissed the district's complaint, holding that the complaint offered only conclusory allegations of anticompetitive effects.

Proving any of the harms alleged in the California complaint is likely to be challenging under the federal consumer welfare standard. The dismissal by the trial court of the district's complaint shows the difficulties that California would face if the case were in the federal courts. Thus, it seems likely that the California attorney general may be trying to avoid the federal consumer welfare standard by bringing the case in the Superior Court of the State of California in the County of San Francisco.

Many states have their own antitrust laws. Indeed, some states enacted antitrust laws before any of the federal antitrust laws existed. These state laws generally operate in tandem with federal law and without federal preemption, even when there are some differences. States' antitrust authority is independent of the federal government's, which means that states may bring their own antitrust cases even if the federal antitrust enforcers choose not to pursue antitrust claims.¹⁷

States took on a larger role in enforcing federal antitrust law in the 1970s, after Congress passed the Hart-Scott-Rodino Antitrust Improvements (HSR) Act. The HSR Act authorized state attorneys general to bring federal antitrust suits on behalf of individuals residing within their states. These lawsuits are known as "parens patriae" suits.

As a result of the HSR Act, states can bring antitrust enforcement actions under both federal law and their own state antitrust laws. Still, states usually choose to bring federal parens patriae claims rather than pursue the same claims under their state laws because federal law provides a robust body of case law to guide courts and litigants. A state's bringing a case instead under its own antitrust laws should raise questions about whether the state is pursuing another agenda that does not depend on helping consumers.

If the California attorney general were to have brought its case in federal court, California could have won the case only if they had shown that consumers on the Amazon website were actually hurt by the Amazon price parity policy.

In this way, the consumer welfare standard provides an important check on enforcers trying to pick winners and losers according to their own personal criteria. The consumer welfare standard focuses on whether the conduct being reviewed makes consumers better or worse off, and the intent is to prevent enforcers' own agendas from creeping in to the decision.

CALIFORNIA COURTS HAVE BEEN WILLING TO IGNORE THE CONSUMER WELFARE STANDARD

Unlike the federal courts (so far), California courts have shown a willingness to set aside the consumer welfare standard in order to achieve their desired outcomes. Most notably, in *ABC International Traders v. Matsushita*, the plaintiffs alleged that certain policies by an upstream supplier treated some middle-level distributors differently than others, which the plaintiffs claimed was an antitrust violation.¹⁸ The California Supreme Court showed little interest in how the policies may have had a valid economic justification (i.e., that they benefitted final consumers). Instead, the majority acknowledged that it was applying a different standard than that used by the federal courts use and ruled that the interests of the distributors trumped the interest of electronics consumers. In doing so, the California Supreme Court protected competitors rather than consumers and competition.¹⁹

California Supreme Court Justice Janice Rogers Brown made the key point about how California's interpretation of the state antitrust law in *ABC International Traders* is not founded in the consumer welfare standard. As she said in her dissent, "this case involves competition among distributors of the same product, competition that cannot conceivably have any significant effect on the touchstones of antitrust policy—interbrand competition, the structure of competitive markets, and the ultimate economic welfare of the California consumer."²⁰

THE DANGER IN CALIFORNIA PURSUING A CLAIM NOT BASED ON THE CONSUMER WELFARE STANDARD

Is the California attorney general pursuing a case against Amazon based on a political agenda that will lead to harm to Amazon shoppers? At this point, the answer is not clear. But the general tone of the California complaint and the press coverage of it appears to suggest that this could be a politicized prosecution aimed at punishing Amazon rather than protecting consumers. For example, during a news conference announcing the lawsuit, Attorney General Bonta said that the lawsuit is a message to other companies who "illegally bend the market at the expense of California consumers, small business owners and the economy."²¹ He also said that he hopes the California legislature will introduce new legislation cracking down on business tactics that discourage competition, indicating that he believes that he should not be bound by the consumer welfare standard when he brings antitrust cases.²²

Even if the California complaint against Amazon is not politicized antitrust enforcement in and of itself, it may be opening the door to politicized antitrust at the state level. States or other political actors may find it politically advantageous to bring cases using standards that are not based on the federal consumer welfare standard. Doing so takes threatens to take America back to the days when Justice Potter Stewart said the only principle he can see is that the government always wins.

Failing to follow the consumer welfare standard can easily, and perhaps inevitably, lead to unprincipled antitrust enforcement. As a group of antitrust scholars points out in a recent paper, by establishing a clear and singular objective, "the consumer welfare standard abandons the use of vague tests that incorporate multiple, and often contradictory, social and political goals that fail to meaningfully cabin discretion and thus ultimately permit decisionmakers to reach almost any result they desire."²³

Since antitrust laws also allow for private enforcement, not adhering to the consumer welfare standard allows businesses to sue other businesses even when consumers are not harmed by the conduct in question. Allowing such cases to go forward undermines the clear statement by the US Supreme Court that the antitrust laws "were enacted for 'the protection of competition, not competitors.'"²⁴ Justice Brown noted this concern in her dissent in *ABC International Traders* when she said, "I fear today's decision will not only eliminate price discounts as a means of enhanc-

ing competition; it will encourage precisely the kind of vexatious and costly litigation which serves only to burden the economy.”²⁵

CONCLUSION

While it is possible that the California attorney general can identify harm to consumers from Amazon’s price parity policy, there are good reasons to believe that the California complaint is targeting conduct by Amazon that may actually be beneficial for consumers and competition. If the case is evaluated by a court under the consumer welfare standard, the litigation process will reveal whether Amazon’s price parity policy helps or hurts consumers. But if the California attorney general prosecutes the case on the basis of Amazon being too big and successful, and a California court agrees, there may not be a clear answer on how the price parity policy affects consumers.

Justice Brown’s concerns raised in her dissent in the *ABC International Traders* case are apt as California goes forward with its lawsuit against Amazon under California antitrust law. A victory by the California attorney general that is not based on the consumer welfare standard will undermine the principle that antitrust decisions should be based on economic analysis rather than political considerations. If California wins in court, more weaponizing of antitrust to target companies for their size is likely to follow. This will only encourage costly litigation slowing economic growth and further weaken the American economy.

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NOTES

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3. “US Tech Antitrust Investigation Tracker,” Thomson Reuters Practical Law, accessed November 25, 2022, <https://content.next.westlaw.com/practical-law/document/1debbae6a11e9adfea82903531a62/US-Tech-Antitrust-Investigation-Tracker>.

4. United States v. Von's Grocery Co., 384 U.S. 270, 301 (1966) (Stewart & Harlan, JJ, dissenting).
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6. Eric A. Posner, "The Rise of the Labor-Antitrust Movement," *CPI Columns*, Competition Policy International, November 29, 2021.
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10. *Brown Shoe Co. v. United States*, 370 U.S. 294, 320 (1962), quoted in *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.* (429 U.S. 477, 1977).
11. Robert H. Bork, *The Antitrust Paradox: A Policy at War with Itself* (New York: Basic Books, 1978), 66, quoted in *Reiter v. Sonotone Corp.*, 442 U.S. 330 (1979).
12. A more systematic explanation of the intellectual foundation for the consumer welfare standard can be found in Elyse Dorsey et al., "Consumer Welfare & the Rule of Law: The Case Against the New Populist Antitrust Movement," *Pepperdine Law Review* 47, no. 4 (2020): 874–77.
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15. *California v. Amazon, Inc.*, CGC-22-601826, 77 (Cal. App. Dep't Super. Ct. 2022).
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17. For a more complete discussion of the law and history of state antitrust, see Eric Peterson and Ted Bolema, *The Proper Role for States in Antitrust Lawsuits* (New Orleans, LA: Pelican Institute, 2022), 19–25.
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