

Resale Price Maintenance and the Rule of Reason

Resale price maintenance (RPM) is a “vertical” agreement controlling the price at which retailers or other distributors can sell the products of a manufacturer or other supplier. In 1911, the Supreme Court declared that minimum RPM is a *per se* violation of Section 1 of the Sherman Act. *Dr. Miles Medical Co. v. John D. Park and Sons*, 220 U.S. 373 (1911). The Court concluded that “vertical” price agreements are functionally equivalent to, and should be treated the same as, “horizontal” price agreements among competitors.

While *Dr. Miles* has been one of the Court’s longest lived antitrust decisions, it has been circumscribed in various ways. For example, the Court overruled its own precedent in 1977 to hold that vertical **non-price** restraints on distribution are **not** *per se* illegal. *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977). And the Court reversed its own precedent again in 1997 to declare that **maximum** resale price maintenance schemes are **not** *per se* illegal. *State Oil v. Khan*, 522 U.S. 3 (1997). In addition, manufacturers can often control minimum resale prices without an unlawful agreement that will violate Section 1, for example by integrating vertically, unilaterally terminating cost-cutting retailers, or imposing various non-price restrictions on retailers. These alternative methods of controlling resale prices, however, may impose costs and risks.

After 96 years, the Supreme Court has revisited and reversed *Dr. Miles* in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.* Leegin, a relatively small manufacturer of women’s hand bags and accessories, marketed one of its product lines in small upscale shops and insisted that the shops agree to charge Leegin’s “suggested” retail prices. After retailer PSKS placed Leegin products on sale, Leegin cut off its product shipments and PSKS sued. The trial court excluded Leegin’s expert testimony suggesting that its pricing policy was procompetitive. The trial court also refused to submit a “Rule of Reason” instruction to the jury. Instead, the trial court held that Leegin’s actions were a *per se* violation of Section 1 of the Sherman Act. The Fifth Circuit affirmed on the authority of *Dr. Miles*, but the Supreme Court reversed and remanded.

The Court began with the proposition that *per se* illegality under the antitrust laws should be limited to situations in which the conduct at issue “always or almost always tend[s] to restrict competition and decrease output.” (Quoting *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717, 723 (1988)). After reviewing the relevant economic literature cited by Leegin and various amici, the Court concluded that RPM will does not meet that standard. The Court was careful to point out that RPM **can** be anticompetitive and thus **can** be illegal under Section 1. Accordingly, it did not decide that RPM was *per se* legal but only that it was not *per se* illegal. As a consequence, any given RPM agreement must be subject to a full Rule of Reason analysis to determine its effect on competition.

In a transparent but limited effort to guide lower courts in their Rule of Reason analysis, the Court cited several factors bearing on RPM’s competitive impact. For example, the Court observed that the threat to competition is less if many manufacturers in a given industry resort to the challenged practice, or if the manufacturer or retailers at issue lack market power. Conversely, vertical price restraints are more problematic if “retailers were the impetus for [the practice],” because RPM can be used to support a retailer cartel or to prop up a dominant but inefficient retailer.

The Court declined, however, to offer a thorough template for deciding whether vertical price restraints will impose an unreasonable restraint of trade. Instead, the Court observed:

As courts gain experience considering the effects of these restraints by applying the rule of reason over the course of decisions, they can establish the litigation structure to ensure the rule operates to eliminate anticompetitive restraints from the market and to provide more guidance to businesses. Courts can, for example, devise rules over time for offering proof, or even presumptions where justified, to make the rule of reason a fair and efficient way to prohibit anticompetitive restraints and to promote procompetitive ones.

After describing the various ways in which manufacturers can already control downstream prices without violating Section 1, the Court described *Dr. Miles* as supporting a “flawed antitrust doctrine that serves the interests of lawyers—by creating legal distinctions that operate as traps for the unwary....” *Leegin*, however, failed to provide clear guidance to manufacturers regarding the line between legal and illegal vertical price restraints. As Justice Breyer noted in dissent, “[t]he only safe predictions to make about today’s decision are that it will likely raise the price of goods at retail and that it will create considerable legal turbulence as lower courts seek to develop workable principles.”

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