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Resale Price Maintenance No Longer a Per Se Antitrust Offense: *Leegin Creative Leather Products v. PSKS, Inc.*

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Summary

The plaintiff in *Leegin Creative Leather Products v. PSKS, Inc.* successfully asked the Supreme Court to soften the longstanding treatment of resale price maintenance (RPM, vertical imposition of direct, minimum price restraints) as a *per se* (automatic, and not capable of being justified) antitrust offense. RPM had been so analyzed since the Court decided in 1911 that a manufacturer of patent medicines could not lawfully agree with retailers of its products on the prices at which those products would be sold (*Dr. Miles Medical Company v. John D. Park & Sons Company*, 220 U.S. 373). Such agreements, the Court had said in *Dr. Miles*, constituted both unlawful restraints of trade under the common law, and violations of the Sherman Act's prohibition against "contract[s] or combination[s] ... in restraint of trade" (15 U.S.C. § 1). Leegin's practice of entering into contracts with its retailers of the Brighton line of leather products to set the prices at which the dealers would resell those products was challenged by a discounting retailer whose replacement shipments were terminated; the trial court found a *per se* violation of section 1 (2004 WL 5254322), and the Court of Appeals for the Fifth Circuit affirmed that decision (171 Fed.Appx. 464 (2006)). Leegin argued in the Supreme Court that because RPM may sometimes be pro-consumer (might, for example, allow the retailers to profitably provide extra services desired by some consumers), the practice should not be conclusively presumed unreasonable "without elaborate inquiry as to 'its precise harm or business justification for its use.'" Agreeing with Leegin, the Court overruled *Dr. Miles*, stating that allowing RPM to be analyzed as a Rule of Reason violation (pursuant to which the procompetitive effects of a judicially determined antitrust violation are weighed against the anticompetitive results of the challenged activity) should be allowed: "Notwithstanding the risks of unlawful conduct, it cannot be stated with any degree of confidence that [RPM] always tend[s] to restrict competition ...." 551 U.S. ___, 127 S.Ct. 2705, 2709 (2007), *quoting*, Business Electronics Corp. v. Sharp Electronics Corp., 485 U.S. 717, 723 (1988).

This report will not be updated.

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Background and Context

Resale price maintenance has been called "vertical price fixing" because it involves entities at different levels of the supply/marketing chain. It generally entails an agreement (via formal contract or otherwise) between a manufacturer and a retailer that the dealer will charge some specific price for the manufacturer's products. As such, the agreement is considered a "conspiracy in restraint of trade" in violation of section 1 of the Sherman Act.[1] The practice, particularly when a floor has been set under permissible resale prices (*minimum* RPM), has been considered a *per se* violation of the antitrust laws[2] since 1911, when the Court decided in *Dr. Miles Medical Company v. John D. Park & Sons Company*[3] that such imposition and agreement was not analytically different from an agreement among the dealers themselves to fix their prices, thus depriving consumers of the advantages of competition.

Imposition of *maximum* resale prices (a "ceiling" on permissible resale prices, as opposed to a "floor" below which a price is not permissible) or some other agreement which may *affect* price but does not require any specific level or term, on the other hand, has more recently been analyzed under the more lenient Rule of Reason standard.[4]

Significant inroads in the law of vertical restraints generally were made by three cases decided in the 1970s and 1980s. First, in *Continental T.V., Inc. v. GTE Sylvania Inc.*, the Court distinguished between vertically imposed price and non-price restraints, specifically overruling a barely 10-year-old, and very contentious case.[5] The *Sylvania* Court concluded that it was "appropriate," given the "complex" market impact of non-price vertical restraints, to return to the Rule of Reason analysis for evaluating them (433 U.S. at 51, 52, 59). Then, in two dealer-termination cases, the Court further clarified its thinking on the "proper dividing line between" *per se* vertical price restraints and Rule of Reason non-price restraints. It required the plaintiff in *Monsanto v. Spray-Rite Service Corp.* to provide evidence of activity on the part of the manufacturer and the non-terminated dealer that "tends to exclude the possibility that [they] were acting independently" (465 U.S. 752, 764 (1984)). Finally, in *Business Electronics Corp. v. Sharp Electronics Corp.* the Court determined that neither (1) all of those agreements which *affect* price (because nearly all vertical agreements do), nor (2) all of those which contain the word "price" should be treated as *per se* violations. *Per se* illegality should be reserved for only those restraints that include "some [express or implied] agreement on price or price levels" (485 U.S. 717, 719, 728 (1988)).

Having distinguished between the proper analysis of vertically imposed price and non-price restraints, the Court, in 1997, imposed further, and more direct, delineations in the law of vertical restraints; in *State Oil Co. v. Khan*, a unanimous Court acknowledged that although *maximum*

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[1] 15 U.S.C. § 1. Section 1, as are all of the other sections of the antitrust laws, is almost "constitutionally" brief, and has been judicially interpreted over the years in thousands of pages of case law.

[2] Pursuant to *per se* analysis a court need not look any further than that the action occurred to find a violation; there can never be any justification (*i.e.*, it isn't possible to convert a *per se* offense into a reasonable action (see n. 5, *infra*) with, *e.g.*, "It was necessary because....").

[3] 220 U.S. 373 (1911), hereinafter referred to as *Dr. Miles.*

[4] Pursuant to the Rule of Reason, despite the finding of an antitrust violation, the court may engage in a "balancing" analysis that allows it to consider the reasonableness of the violative action—*i.e.*, whether its competitive harm is outweighed by the procompetitive results, if any.

[5] 433 U.S. 36 (1977), *overruling*, United States v. Arnold Schwinn & Co., 388 U.S. 365 (1967), which had held a manufacturer-imposed, franchise-location restriction to be a *per se* antitrust violation.

RPM might be used "to disguise arrangements to fix *minimum* prices, ... we believe such conduct ... can be appropriately recognized and punished under the rule of reason." Notwithstanding that the *per se* treatment of maximum RPM had been in effect for approximately 30 years, Justice O'Connor noted, the Court had never been confronted with an "unadulterated" maximum RPM arrangement, and so found the "conceptual foundations [of that rule to be] gravely weakened."[6]

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Continuing the erosion of its precedents in the law of vertical restraints/RPM, a divided (5-4) Court overruled *Dr. Miles*, the final barrier to the Rule of Reason treatment of minimum RPM. Justice Kennedy, joined by Chief Justice Roberts and Justices Scalia (who had authored the *Business Electronics* opinion, *supra*, note 1), Thomas and Alito, stated that

> [v]ertical retail-price agreements have either procompetitive or anticompetitive effects, depending on the circumstances in which they were formed; and the limited empirical evidence available does not suggest [that] efficient uses of the agreements are infrequent or hypothetical. 127 S.Ct. at 2709.

Therefore, the opinion continued,

> [a] per se rule should not be adopted for administrative convenience alone. Such rules can be counterproductive, increasing the antitrust system's total cost by prohibiting procompetitive conduct the antitrust laws should encourage. And a *per se* rule cannot be justified by the possibility of higher prices absent a further showing of anticompetitive conduct. The antitrust laws primarily are designed to protect interbrand competition from which lower prices can later result. *Ibid.*

In apparent anticipation of its decision to overrule *Dr. Miles* (notwithstanding the doctrine of precedent known as *stare decisis*, which counsels that prior judicial precedents generally should not be upset), the opinion devoted a number of pages to presentation of its justifications. After acknowledging that "we do not write on a clean slate, for the decision in *Dr. Miles* is almost a century old," Justice Kennedy set out the reasons the majority felt it appropriate to abandon *stare decisis* in this case (127 S.Ct. at 2720). His justifications included first, the fact that even though "concerns about maintaining settled law are strong when the question is one of statutory interpretation," precedents involving the Sherman Act present a lesser compulsion: "The general presumption that legislative changes should be left to Congress has less force with respect to the Sherman Act."[8] Second, the Sherman Act has been considered and approached as a common-law statute, and,

> Just as the common law adapts to modern understanding and greater experience, so too does the Sherman Act's prohibition on 'restraint(s) of trade' evolve to meet the dynamics of present economic conditions. 127 S.Ct. at 2720.

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[6] 522 U.S. 3, 17, 21, 22 (1997), *overruling*, Albrecht v. Herald Co., 390 U.S. 145 (1968), which found that a newspaper publisher had *per se* violated the 15 U.S.C. § 1 prohibition against agreements in restraint of trade when it gave the customers of one of its distributors to another because its distributor had exceeded the publisher's advertised price for its paper.

[7] 551 U.S. ____, 127 S.Ct. 2705 (2007), decided June 28, 2007.

[8] 127 S.Ct. at 2720, *quoting*, State Oil v. Khan, 522 U.S. at 20.

Third, it would create a "chronically schizoid statute" to have an evolving rule of reason that takes into account "new circumstances and new wisdom," but leaves an "immovable" *per se* line that "remains forever fixed where it was."[9] Fourth, there is ample evidence in economic literature that the *per se* rule is not appropriate for use in any RPM context. Fifth, both the Department of Justice and the Federal Trade Commission (FTC)—"the antitrust enforcement agencies with the ability to assess the long-term impacts of resale price maintenance"—have urged that the distinctions between classes of RPM be abandoned.[10] Finally, prior to reviewing its decisions in the cases described in the "Background" portion of this report, as well as others it considered relevant, the Court quoted from a 2000 opinion to note that "we have overruled our precedents when subsequent cases have undermined their doctrinal underpinnings."[11]

Addressing PSKS's argument that when Congress repealed the authorization for state Fair Trade Laws[12] it was, essentially, ratifying the *per se* rule, the Court replied,

> This is not so. The text of the Consumer Goods Pricing Act [P.L. 94-145] did not codify the rule of *per se* illegality for vertical price restraints. It rescinded statutory provisions that made them *per se* legal. Congress once again placed these restraints within the ambit of § 1 of the Sherman Act.... Congress intended § 1 to give courts the ability 'to develop governing principles of law' in the common-law tradition.[13]

The *Leegin* case, therefore, was remanded to the 5th Circuit, which. in turn, remanded to the district court "for proceedings consistent with the Supreme Court's opinion" (498 F.3d 486 (5th Cir. 2007)).

The dissent, written by Justice Breyer and joined by Justices Stevens, Souter and Ginsburg, took issue with the majority's justification for "its departure from ordinary considerations of *stare decisis*...." (127 S.Ct. at 2725). Although the lawfulness of particular practices is often determined pursuant to the Rule of Reason, they acknowledged, there are some practices whose "likely anticompetitive consequences" are either so serious, with so few possible justifications, or whose justifications are "so difficult to prove [that] this Court has imposed a rule of *per se* unlawfulness—a rule that instructs courts to find the practice unlawful all (or nearly all) of the time" (127 S.Ct. at 2726). The "upshot" of ample economic evidence that RPM can result and has resulted in increased consumer prices,[14] as well as the other side of the argument—that RPM can

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[9] 127 S.Ct. at 2721, *quoting*, National Society of Professional Engineers v. U.S., 435 U.S. 679, 688 (1978), and *Business Electronics, supra,* note 1, at 732.

[10] The Antitrust Division of the Department of Justice had argued in its brief as *amicus curiae* on behalf of *Monsanto, supra*, p. 2, that the Rule of Reason should be used to analyze all instances of RPM. Between the filing of that brief and oral argument in the case (William Baxter, then Assistant Attorney general in charge of the Antitrust Division, presented the oral *amicus* argument), Congress enacted P.L. 98-166, "Departments of Commerce, Justice, and State, the Judiciary, and Related Agencies Appropriation Act, 1984," which contained a proviso that prohibited the Division from expending any of the appropriated funds to make that argument.

[11] 127 S.Ct. at 2721, *quoting*, Dickerson v. U.S., 530 U.S. 428, 443 (2000).

[12] "Fair Trade Laws" were the products of provisos added in 1937 (to section 1 of the Sherman Act) by the Miller-Tydings Act (Public, No. 314, Aug. 17, 1937, ch. 690, Title VIII, § 1, 50 Stat. 693); and in 1952 (to section 5 of the FTC Act) by the McGuire Act (Public Law 542, July 14, 1952, ch. 745, § 2, 66 Stat. 631). Notwithstanding the antitrust law prohibition against "restraint of trade," they permitted (but did not require) the states to enact "fair trade" laws in order to allow manufacturers to enter into agreements with their retailers setting the price(s) at which goods could be sold to the public. The 1952 law further allowed a manufacturer to require *all* sellers of his product(s) in a given state to sell at his established fair trade price if any *one* seller in that state had signed a so-called "fair trade" agreement.

[13] 127 S.Ct. at 2723, 2724, *quoting*, Texas Industries, Inc. v. Radcliff Materials, Inc., 451 U.S. 630, 643 (1981).

[14] Including that from the Department of Justice and the FTC (both of whom advocated a Rule of Reason approach in (continued...)

be beneficial to consumers[15]—leads Justice Breyer to "ask such questions as, how often are harms or benefits likely to occur? How easy is it to separate the beneficial sheep from the antitrust goats?" (127 S.Ct. at 2729).

Moreover, the dissent continued, while it is rational to allow economic discussions to inform antitrust analysis, there is a significant difference between recognizing that economics is a discipline which necessarily contains conflicting views and abandoning the necessity for antitrust law to be administered in such a way as to provide adequate certainty in the "content of rules and precedents" to be applied by the courts and used by "lawyers advising their clients" (127 S.Ct. at 2729). The "special advantages" of a "bright-line rule" they suggested, also might include the potential unfairness and impracticality of pursuing certain potentially criminal offenses (127 S.Ct. at 2731). In its reply to the majority's assertion that the Consumer Goods Pricing Act had not "codified" the *per se* rule of RPM, but rather, had merely "intended § 1 to give courts the ability 'to develop governing principles of law' in the common-law tradition," the dissent emphasized that

> Congress did not prohibit this Court from reconsidering the *per se* rule. But enacting major legislation premised upon the existence of that rule constitutes important public reliance upon that rule. And doing so aware of the relevant arguments constitutes even stronger reliance upon the Court's keeping the rule, at least in the absence of some significant change in respect to those arguments.[16]

Finally, the dissent argued, "every relevant factor ... mention[ed]" by Justice Scalia (a member of the Court's majority here), concurring in the judgment of an earlier case decided this Term, *Federal Election Comm'n v. Wisconsin Right to Life, Inc.* (127 S.Ct. 2652, 2007 WL 1804336), "argues [here] against overturning *Dr. Miles*" (127 S.Ct. at 2734). Those reasons are listed and discussed by Justice Breyer at 127 S.Ct. at 2734-2737:

- First, this case (*Leegin) is* statutory, despite the Court's assertion that it is more properly to be considered in the realm of common-law adjudication; therefore, the Court should accord the deference due *stare decisis* concerning cases involving statutory interpretation.
- Second, although "the Court does sometimes overrule cases that it decided wrongly only a reasonably short time ago," *Dr. Miles* is nearly a century old (not to mention that in overruling *Dr. Miles* this decision also serves to overrule every case that has followed or applied it).
- Third, there is no credible argument that keeping the *per se* rule associated with *Dr. Miles* creates or maintains an "'unworkable' legal regime."

(...continued)

this case) presented at or a few years after the time of the 1975 repeal of the authorization for state "fair trade" laws. *See, e.g.,*Hearings on H.R. 2384 [Consumer Goods Pricing Act] before the Subcommittee on Monopolies and Commercial Law of the House Committee on the Judiciary, 94th Cong., 1st sess. at 113-114, 122 (1975); Hearings on S. 408 [the Senate equivalent to S. 2384] before the Subcommittee on Antitrust and Monopoly of the Senate Committee on the Judiciary, 94th Cong., 1st sess. at 170-172, 173, 176-177 (1975); Bureau of Economics Staff Report to the FTC, T. Overstreet, *Resale Price Maintenance: Economic Theories and Empirical Evidence* at 160 (1983).

[15] Cited by the dissent at 127 S.Ct. at 2728-2729, and 2732.

[16] *Id.* at 2732 (*see* n. 15, *supra,* and surrounding text).

- Fourth, overruling *Dr. Miles* "unsettles" the law to a far greater degree than keeping it would.
- Fifth, the "considerable reliance upon the *per se* rule" of *Dr. Miles* that has led to the involvement of property or contract rights in RPM cases "argues against overruling [that case]."
- Sixth, overruling a "rule of law [that] has become 'embedded' in our 'national culture,'" as has the *per se* rule for RPM, is both improper and unwise.

Accordingly, Justice Breyer concluded:

> The only safe predicitions to make about today's decision are that it will likely raise the prices of goods at retail and that it will create considerable legal turbulence as lower courts seek to develop workable principles. I do not believe that the majority has shown new or changed conditions sufficient to warrant overruling a decision of such long standing. All ordinary *stare decisis* considerations indicate the contrary. 127 S.Ct. at 2737.

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