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Commentary

First Do No Harm: The Discount Protection Consumer Protection Act And The Potential Procompetitive Effects Of Resale Price Maintenance

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James A. Wilson

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Few antitrust decisions of the Supreme Court have evoked the rhetorical intensity of *Leegin Creative Leather Products, Inc. v. PSKS, Inc.* ("*Leegin*"), in which the Supreme Court held that minimum resale price maintenance should be judged under a rule-of-reason rather than a per se standard.[1] Senator Herb Kohl has asserted that "[o]ur experience since the *Leegin* decision is giving credence to … fears [that it would imperil discount shopping that consumers have learned to take for granted], and it comes at exactly the wrong time — just as millions of consumer face a serious recession and depend on bargain shopping more than ever to balance the family budget."[2] Federal Trade Commissioner Pamela Jones Harbour has stated that, "[i]n these tough economic times, it is especially wrong to saddle consumers with higher prices for daily necessities, with no countervailing benefits." [3] Thirty-five state attorneys general have urged Congress to repeal the holding of *Leegin* on the ground that "[a]dvocates of RPM have failed to produce any empirical evidence to show that minimum RPM agreements provide consumer benefits that offset these higher consumer prices."[4] Questions regarding *Leegin* even made their way into the recent confirmation hearing for Judge Sonia Sotomayor.[5]

Certainly *Leegin* involved the rejection of a long-standing precedent. But, contrary to the rhetoric surrounding the decision, it represents neither a radical change in substantive antitrust law nor a rejection of common sense economics. Rather, *Leegin* simply demonstrates a skepticism toward per se rules that has existed for decades, and a willingness to evaluate precedent in light of evolving economic understandings.

Notwithstanding the rhetoric surrounding *Leegin*, if minimum resale price sometimes has procompetitive effects, repealing its holding then will harm consumers in those circumstances when its use is procompetitive. Because the evidence is substantial and convincing that resale price maintenance in at least some circumstances has precompetitive effects, legislation which would reimpose a per se rule of illegality would harm rather than benefit consumers.

A. Resale Price Maintenance And The *Leegin* Decision

In *Dr. Miles Medical Co. v. John D. Park & Sons Co.*,[6] the Supreme Court established the rule that it is per se illegal for a manufacturer to agree with its distributor to set the minimum price the distributor can charge for the manufacturer's goods. The Supreme Court based its analysis on the common law's prohibitions

on restraints on the alienation of property. Eight years after *Dr. Miles*, however, the Supreme Court in *Colgate* generally allowed a supplier unilaterally to adopt and enforce a policy of refusing to deal with discounters because such a unilateral decision did not involve the agreement necessary for a Section 1 violation.[7]

Adding to the complexity in evaluating historical evidence regarding the impact of the prohibition against resale price maintenance, in 1937, Congress passed the Miller-Tydings Fair Trade Act.[8] This Act, which remained in effect until 1975,[9] made vertical price restraints legal if authorized by a state fair trade law. Many of these state statutes allowed a resale price maintenance agreement with one retailer in a state to bind all other retailers, whether the other retailers agreed or not. Thus, from 1937 through 1975, in many states, resale price maintenance was lawful in a number of states, and in many circumstances, compelled by law.

Even after 1975, moreover, manufacturers using the *Colgate* doctrine had a variety tools available to prevent discounting by distributors and retailers: termination of discounting distributors or retailers, suggested resale prices and promotional allowances were all found to avoid the per se treatment required of minimum resale price maintenance under *Dr. Miles*.[10] In 1997, the Supreme Court overturned the per se rule against **maximum** resale price maintenance,[11] which gave further comfort to the view that absent a nake agreement setting a minimum resale price, vertical practices impacting price would be view under the rule-of-reason.

In *Leegin*, the Supreme Court followed the premise that vertical restrains on price can have procompetitive as well as anticompetitive effects to its logical conclusion. The majority opinion starts from the premise that "[t]he rule of reason is the accepted standard for testing whether a practice restrains trade in violation of §1."[12] Accordingly, the Supreme Court concluded that a per se rule is appropriate "only if courts can predict with confidence that [the restraint] would be invalidated in all or almost all instances under the rule of reason . . . ."[13] Therefore, per se categorizations are reserved for restraints "that would always or almost always tend to restrict competition and decrease output."[14]

The majority concluded that minimum resale price maintenance can have either procompetitive or anticompetitive effects, depending upon the circumstances in which they are formed." In some circumstances:

> A single manufacturer's use of vertical price restraints tends to eliminate intrabrand price competition; this in turn encourages retailers to invest in tangible or intangible services or promotional efforts that aid the manufacturer's position as against rival manufacturers. Resale price maintenance also has the potential to give consumers more options so that they can choose among low-price, low-service brands; high-price, high-service brands; and brands that fall in between.[15]

In other circumstances, the majority recognized that resale price maintenance agreements may also be used to obtain monopoly profits or to facilitate cartels at the supplier or retailer levels.[16] However, it concluded on balance that "[a]s the [per se] rule would proscribe a significant amount of procompetitive conduct, these agreements appear ill suited for per se condemnation."[17]

Further, the majority recognized that the *Colgate* decision and application of a per se rule created an anomalous set of rules governing discounting restrictions:

> The manufacturer has a number of legitimate options to achieve benefits similar to those provided by vertical price restraints. A manufacturer can exercise its *Colgate* right to refuse to deal with retailers that do not follow its suggested prices. *See* 250 U.S. at 307. The economic effects of unilateral and concerted price setting are in general the same.[18]

As a result of this dichotomy, prior to *Leegin*, suppliers seeking to implement a minimum resale pricing policy have spent considerable time and effort seeking to establish that those programs were not the subject of an explicit agreement or even tacit understanding between them and their distributors. Indeed, the majority recognized that vertical price restraints may be preferable from a competitive standpoint to reliance on *Colgate* or on vertical

non-price restraints in some instances. [19]

B. Attempts At Legislative Repeal Of *Leegin*

As noted above, the *Leegin* decision was almost immediately decried as an abandonment of the rule of stare decisis and good antitrust policy. Legislation is pending in both houses of Congress to repeal the holding of *Leegin* through enactment of an amendment to Section 1 of the Sherman Act.[20] Under the Senate bill, Section 1 of the Sherman Act would be amended by adding the following prohibition:

> Any contract, combination, conspiracy or agreement setting a minimum price below which a product or service cannot be sold by a retailer, wholesaler, or distributor shall violate this Act.[21]

Under the House bill a similar prohibition would be added as a stand alone provision of the antitrust laws:

> Any agreement setting a price below which a product or service cannot be sold by a retailer, wholesaler, or distributor shall violate section 1 of the Sherman Act.[22]

Both houses have held hearing on these bills, which enjoy the support of numerous state attorneys general and at least one Federal Trade Commissioner, Pamela Jones Harbour.

Supporters of legislative repeal of the *Leegin* holding have raised a number of arguments supporting this legislation:

- Resale price maintenance always results in a price increase of the product to consumers;
- Rule-of-reason treatment amounts to a rule of per se legality;
- The absence of proof of procompetitive effects from resale price maintenance;
- The potential for resale price maintenance to be used to cover or enhance cartels or monopolistic conduct; and
- The prohibitions against resale price maintenance in other jurisdictions.[23]

While these arguments have significant political appeal, none provide a sound basis for reimposing a per se rule of illegality on minimum resale price maintenance.

C. Killing Consumers With Kindness: How Repeal Of *Leegin* Will Harm Consumers

The obvious different between per se and rule of reason treatment of a competitive restraint is that per se treatment does not allow consideration of proof that a practice under the circumstances of a particular case is procompetitive (or at least competitively neutral), while rule-of-reason treatment does. Per se rules provide clear guidance as to what conduct is illegal under the antitrust laws. However, they do so at the sacrifice of consumers if they are applied to a practice that has procompetitive effects. For this simple reason, the Supreme Court has made clear that the normal analytic framework in an antirust case should be the rule-of-reason.

RPM Always Results In An Increase In Prices To Consumers

Proponents of legislative repeal of *Leegin* have frequently asserted that at least with respect to the particular product that is subject to minimum resale price maintenance, consumers always pay a higher price if resale price maintenance is allowed than if it is prohibited.[24] On its fact, this assertion has some obvious appeal — after all, the resale price maintenance itself sets a floor below which the product could not be sold. How then could resale price maintenance not raise the price?

The problematic assumption in this assertion, however, is that a manufacturer who cannot engage in resale price maintenance will not adopt an alternative strategy to gain the perceived benefits (e.g., avoiding freeriding, giving incentive to establish service organizations, preserving brand reputation) sought to be gained by establishing a minimum resale price. The real measure of whether resale price maintenance increases price is by comparison to the other alternatives available to the manufacturer, not by comparison to the manufacturer giving up on attaining those perceived benefits. In a market in which inter-brand competition exists, of course, the manufacturers has significant incentive to choose the option that achieves its goals at the lowest cost to consumers. The claim that resale price maintenance always raises

prices rests on a false comparison.

The Rule Of Reason Amounts To A Rule Of Per Se Legality

Another frequent claim in the debate over repeal of the *Leegin* holding is that adoption of a rule-of-reason standard amounts to a rule of per se legality because it is too difficult for the government or a private plaintiff to win a rule-of-reason case.[25] As the Supreme Court pointed out in *Leegin*, the rule-of- reason is the normal standard for evaluating a competitive restraint — thus, if rule-of-reason amounts to a de facto rule of per se legality, than much broader issues of the meaningfulness of the antitrust standards exists. Obviously, room for debate exists as to how the rule-of-reason should apply to resale price maintenance. However, if (as proponents of the legislation have claimed) there is no proof that resale price maintenance is ever procompetitive, proving a rule-of-reason case in this area should be particularly easy. On the other hand, if such benefits to consumers do exist is some cases, they should not be lightly disregarded.

The Absence Of Proof Of Procompetitive Effects From Resale Price Maintenance

While proponents of repeal of *Leegin* have asserted that there is no proof that resale price maintenance has procompetitive effects, the economic literature weighs heavily against condemning all minimum resale price agreements to per se illegality.[26] This economic literature strongly suggests that minimum resale price maintenance is more often adopted to serve the interests of manufacturers in achieving efficiencies in distribution than to serve the interests of dealers in assuring their margins. Of course, plaintiffs are perfectly free to prove this economic analysis wrong in any given case — presuming it wrong, however, deprives consumers of benefits mainstream economics suggest they will frequently receive.

The Potential For Resale Price Maintenance To Be Used To Cover Or Enhance Cartels Or Monopolistic Conduct

The Supreme Court in *Leegin* itself recognized that resale price maintenance is not always procompetitive. However, the potential for anticompetitive effects has never been grounds for a per se rule. Like concerns about the application of the rule-of-reason, the concern that resale price maintenance can be used to cover or enhance cartels or monopolistic conduct fundamentally rests upon a doubt that the antitrust laws are up to the task of preventing anticompetitive conduct.

The Prohibitions Against Resale Price Maintenance In Other Jurisdictions

The U.S. antitrust laws are not patterned after those of other countries because the U.S. had antitrust laws in place, with a rich and responsive body of judicial decisions, long before these other countries did. Experience has shown that the antitrust laws of the European Union and its member nations have been converging with those of the U.S., not the other way around. One reason is that because the U.S. antitrust laws have been in place for such a long period of time, these and other countries can learn from the long term U.S. experience.

Notwithstanding considerable rhetoric to the contrary, the Supreme Court's decision in *Leegin* does not depart from the basic tenet that protection of competition is the goal of the antitrust laws. Repeal of *Leegin* would deprive consumers of procompetitive conduct that ultimately benefits them. Keeping the rule-of-reason treatment of resale price maintenance in place is the best way for Congress to protect consumers.

Endnotes

1. 551 U.S. 877 (2007).

2. Statement of Senator Herb Kohl at hearing of the Senate Judiciary Committee, Subcommittee on Antitrust, Competition Policy and Consumer Rights, "The Discount Pricing Consumer Protection Act: Do We Need to Restore the Ban on Vertical Price Fixing?" (May 19, 2009), available at http://judiciary.senate.gov/hearings/testimony.cfm?id=3854&wit_id=470 [hereinafter "Kohl Statement"].

3. Testimony of Commissioner Pamela Jones Harbour at hearing of the Senate Judiciary Committee, Subcommittee on Antitrust, Competition Policy and Consumer Rights, "The Discount Pricing Consumer Protection Act: Do We Need to Restore the Ban on Vertical Price Fixing?" (May 19, 2009), available at http://judiciary.

senate.gov/hearings/testimony.cfm?id=3854&wit_id=7935 [hereinafter "Harbour Testimony"].

4. Letter of 35 State Attorneys General Supporting the Discount Pricing Consumer Protection Act available at http://www.naag.org/assets/files/pdf/signons/antitrust.AG_Letter_Supporting_S2261.pdf [hereinafter "State Attorneys General Letter"].

5. Senator Kohl ask Judge Sotomayor: "Do you think it was appropriate for the Supreme Court, by judicial fiat, to overturn a nearly century-old decision on the meaning of the Sherman Act that businesses and consumers had come to rely on and which had been never altered by Congress?" See Transcript of Sotomayor Confirmation Hearings, Day 2, at page 18, available at http://www.nytimes.com/2009/07/14/us/politics/14confirm-text.html?pagewanted=18.

6. 220 U.S. 373 (1911).

7. *United States v. Colgate & Co.,* 250 U.S. 300 (1919).

8. 50 Stat. 693.

9. The Miller-Tydings Fair Trade Act was repealed by the Consumer Goods Pricing Act, 89 Stat. 801.

10. *See generally* ABA Section of Antirust Law, Antitrust Law Developments (6th ed.) at 137-44 (2007)

11. *State Oil Co. v. Khan*, 522 U.S. 3 (1997).

12. 551 U.S. at ___, 127 S.Ct. at 2712.

13. *Id*. at 2713.

14. *Id. (*quoting *Business Elec. Corp. v. Sharp Elec. Corp.*, 485 U.S. 717, 723 (1988)).

15. *Id*. at 2716.

16. *Id*. at 2717.

17. *Id*. at 2717-18.

18. *Id*. at 2722.

19. *Id*. at 2722-23.

20. *See* S. 148 (introduced on Jan. 6, 2009 by Sen. Kohl), available at http://www.thomas.gov/cgi-bin/query/z?c111:S.148:; H.R. 3190 (introduced on July 13, 2009 by Rep. Hank Johnson), available at http://www.thomas.gov/cgi-bin/query/z?c111:H.R.3190.)

21. S. 148.

22. H.R. 3190.

23. *See supra* notes 2-5.

24. *See* State Attorneys General Letter, *supra* n. 5.

25. *See* Harbour Testimony, *supra* n. 4, at 10-11.

26. *See generally* ABA SECTION OF ANTITRUST LAW, ANTITRUST LAW AND ECONOMICS OF PRODUCT DISTRIBUTION 37-76 (2006) ("the bulk of the economic literature on [minimum resale price maintenance] . . . suggests that [minimum resale price maintenance] is more likely to be used to enhance efficiency than for anticompetitive purposes"). ■

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