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U.S. Supreme Court Issues Important Ruling on Resale Price Maintenance

The United States Supreme Court issued an important antitrust decision on June 28, 2007, in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, No. 06-480, http://www.supremecourtus.gov/opinions/06pdf/06-480.pdf. The Court, by a 5-4 majority, overruled a long-standing doctrine that minimum resale price maintenance (RPM) is per se illegal under federal antitrust law, and held instead that the rule of reason applies to such conduct. The Court issued similar rulings in 1977 for non-price distribution restraints (*Continental TV v. GTE Sylvania*), and in 1997 for maximum RPM (*State Oil v. Khan*), in each case shifting from the per se rule to the rule of reason.

Under the per se rule, the plaintiff was not required to prove that minimum RPM had an actual anticompetitive effect in the market for the defendant's product, and the defendant was not permitted to show that the conduct was justified due to efficiencies or other procompetitive benefits. Now, the plaintiff must allege and prove an actual harm to competition, and the defendant may assert business justifications and other defenses.

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Case Summary

Leegin is a small leather goods manufacturer that adopted a minimum RPM policy and obtained agreements from retailers to abide by the policy. PSKS is a retailer who initially agreed to Leegin's policy but later discounted its retail prices, and Leegin stopped selling to PSKS after it learned of this conduct. After a jury trial obtained a judgment of nearly $4 million in treble damages and attorney's fees, PSKS challenged the termination in court under the per se rule. The trial court excluded Leegin's expert evidence on the procompetitive benefits of its policy, and the court of appeals affirmed the judgment in an unpublished opinion, ruling that the lower courts were bound to apply the per se rule.

The Supreme Court acknowledged that the per se rule against minimum RPM stood for nearly a century following its adoption in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, but noted that the economics literature now is replete with procompetitive justifications for manufacturers' use of such programs, similar to those for other vertical restraints. The Court concluded that, although minimum RPM may present risks of anticompetitive harm, the rule of reason should be used to test whether this has occurred. The Court expressed confidence that, through application of the rule of reason, lower courts will establish litigation structure to eliminate anticompetitive restraints from the market and provide more guidance to businesses.

Impact of Decision

The practical impact of the Court's ruling is potentially significant, with important caveats. Suppliers may conclude that they now may enter into explicit agreements with resellers to adhere to a minimum RPM program, particularly in market settings where the supplier faces significant interbrand competition. In the past, suppliers that wished to maintain resale price levels for procompetitive reasons have labored to devise ways to suggest minimum resale prices, but avoid an actual agreement with resellers to adhere to those prices. Such programs are fraught with practical risks because courts have held that an agreement on minimum resale prices can be inferred from circumstantial evidence, such as the interactions between the supplier and its reseller customers following complaints about discounting below suggested price levels.

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Business commentators note that minimum RPM programs may help suppliers position their products in smaller specialty channels, but that large mass merchandisers are unlikely to accept or follow such programs. Whether this is true remains to be seen, as suppliers and resellers adapt to the greater freedom that the rule of reason portends.

Proceed With Caution

Important caveats remain, however, and counsel in favor of a cautious approach with minimum RPM programs. Most important is that, for claims under state antitrust statutes, courts may continue to apply a per se prohibition, notwithstanding the ruling in *Leegin*. Although many state courts follow federal precedent in interpreting state antitrust statutes, some courts may be reluctant to follow a decision that overrules a century-old precedent, particularly a ruling supported by a bare 5–4 majority.

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Importantly, the National Association of Attorneys General (NAAG), in its Vertical Restraint Guidelines, still describes both minimum and maximum RPM as per se illegal. See NAAG Guideline § 2.1, at http://www.naag.org/assets/files/pdf/at-vrest_guidelines.pdf. NAAG did not modify this policy statement after the Supreme Court ruled in *Khan* that maximum RPM should be analyzed under the rule of reason, although some time later a NAAG spokesperson commented that NAAG rarely, if ever, challenged such conduct.

Minimum RPM programs present a greater risk of continued state enforcement, however, because state attorneys general have pursued a number of enforcement actions in recent years against such conduct, including actions against Ty, Inc. (1997), Zeneca, Inc. (1997), American Cyanamid Co. (1997), Nine West Group, Inc. (2000), Salton, Inc. (2002), and Cascade Yarns, Inc. (2005). *See* http://www.naag.org/antitrust/search/results.php?q=resale+price+maintenance. Suppliers may be wary of standing in the vanguard to test whether state courts and state enforcers will accept the reasoning of the majority in *Leegin*.

Suppliers and resellers also must be mindful that the rule of reason is not a rule of per se legality, even though, in many market settings, it presents a formidable obstacle to plaintiffs who seek to challenge minimum RPM programs. To prevail under the rule of reason, the plaintiff must show that minimum RPM is the product of a contract, combination, or conspiracy in restraint of trade, and has caused (or threatened for injunctive relief) an actual adverse effect on competition in the relevant market. To do so, the plaintiff may be required to show that the defendants possess market

power. In market settings where there are many suppliers and vigorous interbrand competition, minimum RPM programs may present little or no threat to competition, and commensurately small legal risk to a supplier and cooperating resellers.

The Supreme Court also expressed concern that minimum RPM programs may facilitate (or reveal) horizontal collusion among interbrand rivals. Such horizontal conduct may still be per se illegal, notwithstanding the decision in *Leegin*.

The ruling in *Leegin* marks a new era in which all vertical distribution restraints now will be analyzed under the rule of reason, at least for federal antitrust claims. Nevertheless, minimum RPM programs continue to present potentially significant risks, and businesses that seek to use or revise resale pricing programs are well-served to seek legal guidance and proceed with caution as courts and government enforcers adapt to this new environment.

If you have any questions or wish to discuss this topic further, please contact the editor, Gregory G. Wrobel at 312/609-7722, gwrobel@vedderprice.com, Michael J. Waters at 312/609-7726, mwaters@vedderprice.com or any other Vedder Price attorney with whom you have worked.

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