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ANTITRUST PRICE RULES CHANGED

On June 28, the U.S. Supreme Court overruled the antitrust precedent that manufacturers and other wholesale sellers of products were not allowed to set minimum retail prices for their products. Many products have been sold with "Manufacturer's Suggested Retail Prices" (MSRP) since a manufacturer could only suggest retail prices to distributors, dealers and retailers. Now, manufacturers may be able to legally agree on minimum prices with distributors, dealers and retailers.

History

In 1911, the U.S. Supreme Court ruled that all vertical minimum price agreements were per se (automatically) illegal as unlawful agreements to limit competition under the Sherman Antitrust Act of 1890. Although manufacturers and other wholesale resellers were legally permitted to unilaterally and independently establish policies not to sell their products to price discounters, the manufacturers and other wholesale resellers were not legally permitted to enter into agreements on minimum prices with their distributors, dealers or retailers. These distinctions between a legal policy and an illegal agreement are described in the Supreme Court's 2007 opinion as "traps for the unwary."

2007 Decision

In the June 28 decision, Leegin Creative Leather Products, Inc. v. PSKS, Inc. doing business as Kay's Kloset, Leegin designed, manufactured and distributed leather goods and accessories including brand name products. Leegin desired to sell its products through small specialty retail stores that Leegin asserted treat customers better, provide customers more services and make their shopping experiences more satisfactory than do larger chain stores. Kay's Kloset sued Leegin in U.S. District Court in Texas alleging that Leegin had violated the antitrust law by entering into agreements with retailers to charge only those prices set by Leegin. After a jury trial, Kay's Kloset obtained a judgment against Leegin in the amount of $3.975 million, which was affirmed on appeal. Leegin did not dispute that it had entered into vertical price fixing agreements with its retailers. In a 5-4 decision, the Supreme Court reversed the judgment ruling in favor of Leegin holding that vertical minimum retail price agreements should not continue to be treated as per se unlawful. The Court held that its 1911 decision should be overruled and that all vertical price restraints are to be judged by the antitrust rule of reason.

Per Se Illegality vs. Rule of Reason

When conduct is per se illegal under federal antitrust law, no defenses or justifications for the conduct are allowed to be considered. Per se illegal conduct includes horizontal price fixing, bid rigging, and horizontal market division agreements. In contrast, since the June 28 Supreme Court decision, all price and non-price vertical agreements are subject to rule of reason analysis. A rule of reason analysis entails a fact intensive, case-by-case analysis of the agreement at issue taking into account specific information about the relevant business and the agreement's history, nature and effect. In a rule of reason analysis, whether the businesses involved have market power is a significant consideration. The rule of reason analysis distinguishes between agreements with anticompetitive effects harmful to the consumer and agreements stimulating competition in the consumer's best interest.

Under a rule of reason analysis, a vertical price restraint will be found to violate federal antitrust law only if, after weighing all the circumstances, the judge or jury concludes that the vertical price agreement has anticompetitive effects which outweigh the agreement's procompetitive benefits.

If a manufacturer decides to initiate vertical minimum price agreements with its distributors, dealers or retailers, it is advisable that the manufacturer document procompetitive benefits created by such agreements.

This document may be considered "Attorney Advertising" under the rules of some states.
The hiring of a lawyer is an important decision that should not be based solely upon advertisements.

Horizontal price fixing agreements continue to be per se illegal under federal antitrust law. (Horizontal agreements are agreements by competitors.) Illegal horizontal price fixing agreements are subject to substantial civil liability, including treble damages, and significant criminal penalties.

Three Factors

In Leegin, the Supreme Court set forth three factors which should be considered in determining whether an agreement on minimum retail prices between a manufacturer and its retail customer is permitted. The three factors are: (1) How many manufacturers in the industry have minimum retail price agreements? If many competing manufacturers adopt the practice, then, more careful scrutiny is required to determine if the agreements are anticompetitive. If only a few manufacturers adopt minimum retail price agreements, then, the risk that the agreements are anticompetitive is less. (2) Who is the source of the agreement? If there is evidence that a retailer was the impetus for a minimum retail price agreement, there is a greater likelihood that the agreement facilitates an illegal cartel among retailers or supports a dominant, inefficient retailer. By contrast, if a manufacturer adopts the policy independent of retailer pressure, the agreement is less likely to promote anticompetitive conduct. (3) Does a party to the minimum retail price agreement have market power? (For antitrust purposes, "market power" is defined for a seller as the ability profitably to maintain prices above competitive levels for a significant period of time). If a dominant manufacturer possesses market power in the relevant product market and geographic market, there can be a finding that a vertical minimum price agreement is being used for anticompetitive purposes. A manufacturer with market power could be liable under the rule of reason for an unreasonable agreement limiting competition as well as monopolization or attempt to monopolize claims.

State Law

As a cautionary note, the Supreme Court's 2007 decision changes federal antitrust law. However, state antitrust law may continue to treat vertical minimum price agreements as per se illegal under state antitrust law. (As another consideration, New York General Business Law § 369-a provides that any agreement that purports to restrain the purchaser of a product from reselling such product at less than the price stipulated by the manufacturer or producer shall not be legally enforceable.)

Traffic Light Analogy

Using a traffic light analogy – red (stop), yellow (caution) and green (go) – the Leegin decision means that the traffic light for vertical minimum price agreements has changed from red (stop – prohibited conduct) to yellow (you may proceed with caution). The traffic light has not changed from red to green. Some vertical minimum price agreements will be legal, but the consequences of illegality – treble damages plus attorneys' fees – can be devastating to a company. In Leegin, the Supreme Court invited lower courts to develop procedures and standards under the rule of reason in litigated disputes to distinguish legal minimum price agreements from illegal agreements. Manufacturers and other wholesale sellers should proceed with caution (and legal advice) in implementing any vertical minimum price agreements.

The Supreme Court's decision may provide a good reason to review pricing, distribution and marketing strategies. Please contact your BS&K attorney, or one of the attorneys listed below, if you would like BS&K to advise you on the legal aspects of your pricing, distribution and marketing strategies.

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Agreements among competitors which remain per se illegal:

- **Price fixing**
- **Bid rigging**
- **Market division**