

# Reasoning Through the Rule of Reason for RPM

BY THEODORE VOORHEES, JR.

THE ASCENDANCY OF THE ANTITRUST rule of reason continues apace. A 35-year stream of U.S. Supreme Court rulings stating a strong preference for the rule of reason over per se shortcuts remains steady, and the Court has expressed full confidence that federal district courts are up to the task of making the rule work at trial.

But where exactly does this confidence in the lower courts' aptitude for handling rule of reason cases come from? Recent scholarship in this area has found trends, but not ones the Supreme Court would find encouraging. If anything, there seems to be a marked tendency among lower courts to avoid or simplify rather than boldly embrace full rule-of-reason analysis. What seems to be emerging is experimentation with simplifying forms of "structured" reasoning aimed at making the rule of reason workable. It remains to be seen whether that is what the Supreme Court has had in mind.

In *FTC v. Actavis*,<sup>1</sup> the U.S. Supreme Court held that the determination of whether "reverse-payment" settlements between branded and generic pharmaceutical manufacturers are pro- or anticompetitive should be conducted under the rule of reason rather than a standard of presumptive illegality that had been advocated by the Federal Trade Commission. The Court found that settlements of this kind raise many issues and "complexities" for antitrust courts that render use of presumptions or other "quick look" standards inappropriate.<sup>2</sup> Justice Breyer, writing for the majority, concluded that the rule of reason could solve these complexity problems with the help of prudent trial management by district court judges:

As in other areas of law, trial courts can structure antitrust litigation so as to avoid, on the one hand, the use of antitrust theories too abbreviated to permit proper analysis, and, on the other, consideration of every possible fact or theory irrespective of the minimal light it may shed on the basic ques-

tion—that of the presence of significant unjustified anti-competitive consequences."<sup>3</sup>

The *Actavis* Court's assurance that trial courts will be able to develop special litigation "structures" for rule-of-reason cases mirrored a closely similar Supreme Court finding six years ago in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*,<sup>4</sup> albeit in a case where Justice Breyer had dissented. In *Leegin*, a sharply divided court had overturned the 96-year-old *Dr. Miles* rule under which resale price maintenance (RPM) had been deemed per se unlawful. Writing for the *Leegin* court majority, Justice Kennedy determined that the rule of reason would thenceforward govern and expressed confidence that:

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.<sup>5</sup>

As district courts begin to undertake rule-of-reason analyses of reverse-payment cases, it is instructive to ask how "litigation structures" have been developed in RPM cases post-*Leegin* to separate the procompetitive "sheep" from the anticompetitive "goats." Unfortunately, one finds only incomplete answers to this question, even though it has been 15 years since the Supreme Court determined that the antitrust rule of reason should govern maximum RPM,<sup>6</sup> and 6 years since the *Leegin* Court extended this doctrine to minimum RPM.<sup>7</sup> To understand why, it is helpful to review the handling of rule-of-reason cases over a slightly longer period that began with the Supreme Court's milestone ruling in *Continental TV, Inc. v. GTE Sylvania, Inc.*<sup>8</sup>

## The Economics-Driven Shift in Analysis from Presumption Toward Reason: *GTE Sylvania* through *Leegin*

The *GTE Sylvania* decision was possibly the Supreme Court's most important antitrust ruling in the modern era for it was in that case that the Court pronounced that economic analysis would thereafter serve as the core framework

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for determining the lawfulness of restraints on competition. *GTE Sylvania* involved a manufacturer's restrictions on the geographic scope of distributor operations—a kind of vertical restraint that the Court had previously treated as per se unlawful. In rejecting the per se rule for vertical *nonprice* restraints and substituting the antitrust rule of reason, the *GTE Sylvania* decision drew a critical distinction between the competitive effects of vertical restraints on distributors of the manufacturer's own brand (so-called intrabrand competition), and the effects of such restraints on competition with rival manufacturers (so-called interbrand competition). Faced with a territorial restraint that tended to diminish intrabrand competition but nevertheless stood to enhance interbrand competition, the Court ruled in *GTE Sylvania* that interbrand competition is "the primary concern of antitrust law."<sup>9</sup>

With increased interbrand competition as the critical endpoint, the Court then emphasized that modern antitrust economics has identified numerous ways that a manufacturer can use vertical territorial restraints on its distributors to achieve certain quality and service advantages that can make the manufacturer's product more competitive against rival products. The *GTE Sylvania* ruling focused specifically on two categories of these quality advantages that are distinct from the product's price: (1) encouragement of retailer investment in distribution of the manufacturer's brands,<sup>10</sup> and (2) encouragement of retailer promotional activity, service and repair facilities that might not otherwise be provided because of the free-rider problem.<sup>11</sup>

In succeeding years, the Supreme Court has applied the same basic economic tenets of the *GTE Sylvania* ruling to vertical price restraints, first in its 1997 *Khan* decision (involving restraints on maximum RPM) and then in its 2007 *Leegin* decision (involving restraints on minimum RPM). In each instance the Court grounded its ruling on *GTE Sylvania*'s application of modern antitrust economic analysis, the predominant importance of the restraint's effects on interbrand rather than intrabrand competition, and the significant role played by quality/service factors in enhancing interbrand competition. In *Leegin*, the Court observed that RPM "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."<sup>12</sup> RPM can also increase interbrand competition, absent free-riding, in situations where

[i]t may be difficult and inefficient for a manufacturer to make and enforce a contract with a retailer specifying the different services the retailer must perform. Offering the retailer a guaranteed margin and threatening termination if it does not live up to expectations may be the most efficient way to expand the manufacturer's market share by inducing the retailer's performance and allowing it to use its own initiative and experience in providing valuable services.<sup>13</sup>

The Court went on to note that although manufacturers might be able to achieve many of the same quality/service

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advantages by vertically integrating, this might not be as efficient as maintaining independent distributors:

[D]epending on the type of product it sells, a manufacturer might be able to achieve the procompetitive benefits of resale price maintenance by integrating downstream and selling its products directly to consumers. . . . This . . . might lead to inefficient integration that would not otherwise take place, so that consumers must again suffer the consequences of the suboptimal distribution strategy. And integration, unlike vertical price restraints, eliminates all intrabrand competition.<sup>14</sup>

On the strength of these economic rationales, the Court in *Leegin* concluded that agreements setting minimum resale prices no longer should be unlawful per se—a category that under U.S. law is confined to restraints "that would always or almost always tend to restrict competition and decrease output."<sup>15</sup> That did not mean RPM would always be deemed lawful, however, and indeed the Court mentioned several contexts involving horizontal concerted conduct or dominance in which the practice could still be found unlawful. Thus, RPM could have significant anticompetitive effects where it is (a) the product of a conspiracy among suppliers to elevate prices market-wide; (b) imposed by collusion among dealers insisting that the supplier eliminate discounters; (c) imposed by a dominant retailer to impede smaller retailers; or (d) imposed by a dominant supplier in order to discourage retailers from carrying the products of other suppliers.<sup>16</sup>

**How Has the Rule of Reason Actually Worked in Litigation over RPM?**

The combination of the Court's three seminal rulings in *GTE Sylvania*, *Khan*, and *Leegin* set the stage for determining how particular vertical price restraints aimed at securing quality and service enhancements would fare under the antitrust rule of reason in actual litigated cases. So then, how has the rule of reason actually worked in assessing quality/service enhancements, and what actually has happened when particular vertical price restraints used in real world interbrand rivalries were tested in litigation under the antitrust rule of reason? The answer to both questions is that it is still too early to say, given the insufficient track record of litigated vertical price restraint cases, how quality/service factors are

actually measured and how they could or should be balanced against arguably negative competitive effects on price or output.

The Supreme Court has characterized in several ways how the rule of reason is to be applied when assessing a restraint's asserted pro- and anticompetitive effects. For example, in *GTE Sylvania*, the Court has said that all relevant circumstances are to be "weighed."<sup>17</sup> The Court subsequently referred to the utility of examining "countervailing" factors that could possibly enhance competition in the face of restraints that might impede it:

Absent some countervailing procompetitive virtue—such as, for example, the creation of efficiencies in the operation of a market or the provision of goods and services—such an agreement limiting consumer choice by impeding the "ordinary give and take of the market place," cannot be sustained under the Rule of Reason.<sup>18</sup>

Justice Scalia has similarly noted in dictum in a dissenting opinion that the competing pro- and anticompetitive effects are to be "balanced":

Per se rules of antitrust illegality are reserved for those situations where logic and experience show that the risk of injury to competition from the defendant's behavior is so pronounced that it is needless and wasteful to conduct the usual judicial inquiry into the balance between the behavior's procompetitive benefits and its anticompetitive costs.<sup>19</sup>

The Court has also indicated that the various competitive tendencies are to be combined in some way, not specifically delineated, in order to reveal their ultimate net or preponderant directional effect: "[T]he inquiry mandated by the Rule of Reason is whether the challenged agreement is one that promotes competition or one that suppresses competition."<sup>20</sup>

The post-*Khan/Leegin* case law has not yet developed a robust body of analysis demonstrating how the rule of reason will or should be applied in RPM litigation to ascertain "the presence of significant unjustified anticompetitive consequences." Few courts have attempted full rule-of-reason analysis for territorial restraints after *GTE Sylvania* or for RPM after *Khan* and *Leegin*. For minimum RPM restraints,<sup>21</sup> there have been few cases and many ways to avoid rule-of-reason balancing. Although the rule of reason has been applicable to Sherman Act minimum resale price maintenance cases for six years, there are few, if any, instances where courts have conducted weighing, balancing, net effect measurements of pro- and anticompetitive effects, or even burden-shifting. Why is this so?

First, there simply do not appear to have been many instances of contested cases involving minimum RPM. The *Leegin* decision does not appear to have unleashed any great rush among manufacturers to institute mandatory minimum price programs, most likely because they would still face potentially serious claims under the antitrust laws of several states, such as California and Maryland, which still treat minimum resale price maintenance as per se illegal.

Second, in the few post-*Leegin* cases involving minimum RPM that have been contested, none has reached the weighing or balancing stage. This is because courts have found ways to dispose of most such cases before having to conduct burden-shifting, far less full rule-of-reason analysis. Thus, some courts have ordered dismissal after finding that the plaintiff had failed to show any underlying anticompetitive effect to begin with. For example, in *Bel Canto Design, Ltd. v. MSS HiFi, Inc.*,<sup>22</sup> the court granted the defendant's motion to dismiss on multiple grounds, including the plaintiff's failure to plead either the defendant's possession of market power in a proper relevant market or harm to interbrand competition.

In other instances, courts have found ways to avoid full rule-of-reason analysis by dismissing the plaintiffs' claims on elemental grounds, such as failure to meet the threshold requirement of defining a bona fide relevant market.<sup>23</sup>

In the *Leegin* case on remand after the Supreme Court's ruling, the Court of Appeals for the Fifth Circuit observed that even if the plaintiff had alleged a valid relevant market there, plaintiff's theory of harm failed to "recognize that retailers will cease carrying [the manufacturer's] goods if [the manufacturer] imposes onerous requirement that make [its] products difficult to sell" while "robust competition can exist even in the absence of price competition."<sup>24</sup> However, this did not amount to a balancing of evidence of price and quality effects because no such evidence was placed on the judicial scales.

Similarly, in *In re Nine West Group Inc.*,<sup>25</sup> the Federal Trade Commission modified a prior consent decree, which had prohibited minimum RPM, on the grounds that the manufacturer lacked market power and that the impetus for adopting minimum RPM came from the manufacturer alone, not from the retailers. However, the Commission explicitly rejected the manufacturer's assertion that implementing minimum RPM would "increase consumer demand for its products and thereby enhance competition," and therefore no weighing of price and quality effects occurred in that matter either.

In fact, a review of the case law in *Antitrust Law Developments* finds that U.S. courts have more often than not studiously avoided reaching the point of having to clarify this obscure area of the law:

The case law, moreover, provides few examples of attempts to balance because most rule of reason cases do not proceed that far: they usually are resolved when the plaintiff fails to prove a substantial anticompetitive effect or the defendant fails to provide evidence that the restraint is reasonably necessary to achieve a substantial procompetitive effect.<sup>26</sup>

Professor Michael A. Carrier performed a comprehensive survey of post-*Sylvania* rule-of-reason case law in 1999 that assessed the ways federal courts had conducted rule-of-reason balancing during the nearly quarter-century that had elapsed since that decision.<sup>27</sup> Carrier concluded that "in an astonishing 96% of Rule of Reason cases, courts do not balance anything."<sup>28</sup> He noted that an important part of the problem

was the hard fact that the sheer diversity and heterogeneity of competitive effects, both pro- and anti-, defies simple comparisons via mathematical or other systematic measurement: “Can courts balance anticompetitive and procompetitive effects? The odds are against them. For courts rarely will be able to sum up a restraint’s net effect on output or price. By no stretch can we be assured of the results of balancing with mathematical exactitude.”<sup>29</sup>

Carrier published a subsequent survey of rule-of-reason cases decided between February 2, 1999 and May 5, 2009. He found that of 222 decisions that reached a final determination, 215 (96.8%) “were resolved on the grounds that the plaintiff did not prove an anticompetitive effect” and only 5 cases (2.2%) performed balancing.<sup>30</sup> The plaintiff won in only one of the five cases that went through a balancing analysis.<sup>31</sup>

Even the deceptively simple net- or preponderant-directional-effect test suggested by the Supreme Court in *National Society of Professional Engineers* retains the same computational difficulties posed by balancing and weighing individual effects. As Professor Carrier noted in 1999:

A narrower test than the current balancing, for example, may look only to the net effect of the restraint on output. But such an approach will not solve most cases since the competitive effects of restraints do not usually manifest themselves so clearly as to lead to a “net result.”<sup>32</sup>

Carrier asked: “How can courts do it? Doesn’t it require the comparing of apples (e.g., an increase in interbrand competition) and oranges (e.g., a decrease in intrabrand competition)?”<sup>33</sup>

Hence, there is an inescapable methodological difficulty for any court or jury that wishes to weigh, balance, or “net out” all the relevant competitive effects of RPM or other vertical restraints. In these circumstances, Carrier notes that many post-*GTE Sylvania* courts found ways to avoid full rule-of-reason analysis. One of the most popular was by finding that the plaintiff had failed at the threshold stage to demonstrate any anticompetitive effect of the restraint. In territorial and customer restraint cases surveyed by Carrier in 1999, for example: “The courts found that the plaintiff failed to demonstrate a significant anticompetitive effect in 105 out of 118 cases (89%) involving vertical restraints.”<sup>34</sup>

Thus, federal courts in most cases have not reached the difficult—perhaps insoluble—challenge of weighing, balancing, or netting out all possible pro- and anticompetitive features that might be presented in vertical restraint cases, including RPM cases, but that are not amenable to systematic comparison pursuant to standard metrics. Cases have therefore been disposed of in the vast majority of instances by other means that preempt the need for full rule-of-reason assessment. Courts in the few recent RPM cases that have been contested have generally ruled for defendants without engaging in rule-of-reason balancing where they could rule out the main categories of concern related to RPM as noted in the *Leegin* ruling, i.e.:

- where the court could rule out *dominance* concerns, as where the plaintiff failed to show a relevant market in which the defendant exercised market power harmful to competition,<sup>35</sup>
- where the plaintiff failed to show an anticompetitive effect on *interbrand* competition,<sup>36</sup>
- where the court could rule out concerns about *concerted horizontal conduct* at the supplier and retailer levels.<sup>37</sup>

Conversely, in three instances where a federal court has allowed the plaintiff’s RPM claim to proceed (yet without engaging in rule-of-reason balancing), the courts were persuaded by claims that the RPM policy arose due to pressure from a dominant retailer or a possible retailer cartel rather than from the interest of the manufacturer.<sup>38</sup>

In the meantime, a number of commentators have sought to provide guidance. Most have focused on a structured approach that mainly emphasizes shifting burdens of proof rather than explicit “weighing,” “balancing,” or “netting” out of “countervailing” tendencies, though the latter notions do not disappear altogether.

A good example of the structured approach is provided in a paper by Gregory Werden, Senior Economic Counsel in the Antitrust Division of the Department of Justice.<sup>39</sup> Werden categorizes RPM and other vertical restraint cases as “non-suspect,” noting that “we think we know that vertical restraints ‘hold promise of increasing a firm’s efficiency and enabling it to compete more effectively,’ and thus they normally do not harm the competitive process.”<sup>40</sup> Here is a distilled summary of Werden’s proposed three-stage, structured, burden-shifting approach to rule-of-reason analysis in a non-suspect vertical case:

#### *Stage 1—Plaintiff’s Initial Burden*

To carry its initial burden, a plaintiff challenging a non-suspect restraint must demonstrate, inter alia, the potential for a significant anticompetitive effect. For this, the courts generally require a threshold showing of market power. . . . [Alternatively] The plaintiff instead may demonstrate the potential for a restraint to have a significant anticompetitive effect by showing its actual marketplace impact.<sup>41</sup>

#### *Stage 2—Defendant’s Burden*

For non-suspect restraints, the defendant can rebut any showing the plaintiff makes on the potential for significant anticompetitive effects. Market delineation is often a major area of dispute, as are other factors relevant to market power. . . . The defendant should be permitted to dispute not only the factual basis for the plaintiff’s argument but also the economics relied upon . . . . In cases not involving cartel activity, justifications can be important.<sup>42</sup>

#### *Stage 3—The Plaintiff’s Ultimate Burden*

The plaintiff might discredit the justification by showing that the restraint could not accomplish what is claimed of it. The plaintiff might negate the justification by showing that

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a less restrictive alternative would have accomplished what the restraint accomplishes as well or better. The plaintiff also might show that the restraint nevertheless harms competition. . . . In the close cases, the plaintiff almost surely will fail to carry its burden because no analytic apparatus offers the precision necessary for making close calls.<sup>43</sup>

Academic and other commentators have offered their own, somewhat similar proposals for a structured rule-of-reason analysis,<sup>44</sup> and case law analyzing nonprice vertical restraints has provided additional articulations of the burden-shifting approach.<sup>45</sup>

As might be expected, generalities about “weighing” or “balancing” or discerning ultimate “net” directional effect, or even providing a “structured” approach using burden-shifting do not provide highly specific guidance on how the assessment process is actually to be performed in real cases involving countervailing factors that are not easily reduced to quantifiable metrics. And in fact, the U.S. courts have not produced many rulings that offer practical instruction. As the most recent edition of *Antitrust Law Developments* summarized the current situation:

The Supreme Court has provided little guidance about how this balancing process should be conducted, and lower courts have questioned the feasibility of any explicit balancing because offsetting competitive effects often do not lend themselves to easy measurement.<sup>46</sup>

After all, how does one find a common denominator that allows fair comparisons among such disparate concepts as increase in price, increase in output, greater product choice, lower product inventory, better customer service, decline in marketing effort, strengthening of incentives to innovate, increase in distributor investment, reduction in product quality, etc.? Leading commentators have identified the same fundamental fallacy in rule-of-reason “balancing/weighing” methodology as that identified by Michael Carrier above. Professor Herbert Hovenkamp, for example, has observed that “[t]he set of rough judgments we make in antitrust litigation does not even come close to this ‘balancing’ metaphor.”<sup>47</sup>

## Prediction for Future RPM Litigation

I predict that the pattern in RPM case outcomes will persist in U.S. litigation for the foreseeable future. It seems likely that the courts will not attempt to weigh or balance distinct pro- and anticompetitive effects against one another in any specific computational sense, but rather will gradually settle on a structured rule-of-reason analysis as they were invited to do by the *Leegin* majority opinion. They are likely to choose a simplified structured approach similar to the burden-shifting system articulated by Werden and other contemporary commentators. Under this structured analysis there will likely be a relatively simple three-stage test offering the practical equivalent of two safe harbors for RPM in most cases:

### *Stage One—Is There Robust Interbrand Competition?*

The first stage involves a determination whether the plaintiff can demonstrate the existence of a significant harmful effect on competition in the market, which in practical terms will require a showing of harm to interbrand competition. This might occur, for example, if there is evidence that RPM was introduced as the result of horizontal concerted action at either the distributor or manufacturer level. The requisite harmful effects might also be shown if RPM were being practiced by a dominant manufacturer: one who possesses significant market power in the relevant market. If the plaintiff is unable to show these or other comparable harmful encroachments on interbrand competition, however, his case would be dismissed at this first stage.

Another way to understand the likely outcome here is to acknowledge that the existence of robust interbrand competition, or at least the practical inability of the plaintiff to demonstrate the absence or serious diminution of interbrand competition, offers a first safe harbor for manufacturer-imposed RPM. The intuition here is that a rational manufacturer facing robust interbrand competition will prevent its retailers from cutting price *only* if it genuinely believes there is a better way to increase its sales against rival products, most likely by rewarding retailer provision of enhanced services. The manufacturer’s judgment may be wrong, of course, but if so, a robust interbrand market will mete out swift and sure punishment when either consumers unimpressed by expensive services move to lower-price-lower service alternatives<sup>48</sup> or retailers disappointed by unfulfilled promises of service-stimulated sales growth migrate to rival manufacturers.<sup>49</sup>

### *Stage Two—Is There a Facially Plausible Justification for RPM in the Particular Case?*

If the plaintiff can show specific potential harm to interbrand competition in a defined market, however, then the analysis moves to the second stage where the defendant would be required to demonstrate that RPM is justified by actual procompetitive benefit (i.e., not merely theoretical benefit) in its particular case. The procompetitive benefit would likely have to be demonstrated in accordance with a kind of sliding scale to a level of probity commensurate with the strength

of the plaintiff's proof of the factors imposing potential jeopardy to interbrand competition. It would be harder, for example, for a defendant to justify RPM if the case involves a market for commodity products in which the plaintiff is able to show a heightened danger of coordinated conduct among rival producers and the defendant is unable to explain why consumer education and other conventional retail-level services and promotional activities are important to buyers. Conversely, if the market involves complex, highly differentiated products requiring use instructions and valuable retailer-provided services, the procompetitive benefit from RPM would appear to be irrefutable for all practical purposes, if only because no common metric exists to show that an alleged anticompetitive effect weighs more heavily.

Another way to understand this likely outcome is to acknowledge that a second safe harbor exists for manufacturer-imposed RPM when the manufacturer has a good faith-based belief that retailer-supplied services will benefit sales of its products against rivals. The Supreme Court's rulings in *Federation of Dentists* and *Actavis* certainly suggest that the existence alone of a "countervailing procompetitive virtue"<sup>50</sup> or of a rationale demonstrating the restraint is not "unjustified" will trump even "significant . . . anticompetitive consequences."<sup>51</sup>

### *Stage Three—Is the Proffered Justification Pretextual?*

A third stage would allow the plaintiff to attempt to show that the defendant's justifications are irrelevant, lacking in merit, or pretextual, or that the defendant could have achieved its objectives through significantly less restrictive and readily available means.

The foregoing burden-shifting would not necessarily require mathematical weighing or balancing of any individual pro- and anticompetitive effects at any stage. Rather, the defendant could prevail, at least in theory, simply by demonstrating both the bona fides of its objectives in utilizing RPM and that RPM was a reasonable tool for achieving those objectives in the particular market situation. Thus, for example, if the plaintiff were able to demonstrate that the defendant already possessed market power in the relevant market, that would tend to undermine the plausibility of many of the procompetitive benefits that are usually cited in favor of RPM, regardless of any further weighing.

Similarly, the arguable role of concerted action among distributors or rival manufacturers leading to imposition of RPM would call into question the credibility of any argument that RPM was designed to spur distributors to make greater distributional efforts in support of the manufacturer's brands against rival brands. On the other hand, if the plaintiff were unable to identify any specific harm to interbrand competition posed by the defendant's RPM, as occurred in the *Bel Canto Design* case,<sup>52</sup> then any plausible basis for using RPM to motivate distributors to provide enhanced marketing, sales and service effort on behalf of the defendant's product would seem to suffice.

It thus seems likely that an ad hoc convergence between the lower courts' pattern of avoiding rule-of-reason balancing and the apparent practicality of a structured rule-of-reason approach based on burden shifting will progress over the years to come. Perhaps during that interval the Supreme Court will find an opportunity to confront the anomalous situation of its weighing/balancing signals being largely ignored, and further refine the rule-of-reason test so that it conforms more closely to both economics and realities on the ground.

Of course, this does not leave a seller employing RPM free of any discipline. Like audiences at movie theaters and sporting events, retailers and consumers in free, competitive markets are always able to penalize ineffective marketplace behavior the old-fashioned way—by voting with their feet. ■

<sup>1</sup> 133 S. Ct. 2223 (2013).

<sup>2</sup> *Id.* at 2237.

<sup>3</sup> *Id.* at 2238.

<sup>4</sup> 551 U.S. 877 (2007).

<sup>5</sup> *Id.* at 898–99.

<sup>6</sup> See *State Oil Co. v. Khan*, 522 U.S. 3 (1997).

<sup>7</sup> See *Leegin*, 551 U.S. 877.

<sup>8</sup> 433 U.S. 36 (1977).

<sup>9</sup> *Id.* at 52 n.19.

<sup>10</sup> *Id.* at 55 ("For example, new manufacturers and manufacturers entering new markets can use the restrictions in order to induce competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer.").

<sup>11</sup> *Id.* ("Established manufacturers can use them to induce retailers to engage in promotional activities or to provide service and repair facilities necessary to the efficient marketing of their products. . . . The availability and quality of such services affect a manufacturer's goodwill and the competitiveness of his product. Because of market imperfections such as the so-called 'free rider' effect, these services might not be provided by retailers in a purely competitive situation, despite the fact that each retailer's benefit would be greater if all provided the services than if none did.").

The Supreme Court explained the free-rider effect most recently in *Leegin*, 551 U.S. at 890–91 ("Absent vertical price restraints, the retail services that enhance interbrand competition might be underprovided. This is because discounting retailers can free ride on retailers who furnish services and then capture some of the increased demand those services generate.").

<sup>12</sup> *Leegin*, 551 U.S. at 890.

<sup>13</sup> *Id.* at 892.

<sup>14</sup> *Id.* at 903.

<sup>15</sup> *Id.* at 886 (quoting *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717, 723 (1988)).

<sup>16</sup> *Id.* at 892–99; see, e.g., *Toledo Mack Sales & Serv., Inc. v. Mack Trucks, Inc.*, 530 F.3d 208 (3d Cir. 2008) (reversing judgment in favor of defendant and finding that plaintiff should have been allowed to present its case to a jury based on evidence supporting allegations of horizontal agreements among dealers not to compete on price, dealer pressure on the manufacturer, and the manufacturer's possession of market power in two relevant product markets).

<sup>17</sup> *GTE Sylvania*, 433 U.S. at 49; see also *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 761 (1984) (rule of reason "requires a weighing of the relevant circumstances of a case"). The American Bar Association has prepared model jury instructions to be used by courts in guiding juries in the

- application of the antitrust rule of reason. In the latest version of these model jury instructions, published in 2005, the ABA adopted the Supreme Court's "weighing" formulation and added the notion that a restraint will be deemed unreasonable only if it produces a "substantial" excess of harm over benefit: "If the competitive harm substantially outweighs the competitive benefits, then the challenged restraint is unreasonable. If the competitive harm does not substantially outweigh the competitive benefits, then the challenged restraint is not unreasonable." ABA SECTION OF ANTITRUST LAW, MODEL JURY INSTRUCTIONS IN CIVIL ANTITRUST CASES, 2005 Edition Instruction 3d A-12 (2005).
- <sup>18</sup> *FTC v. Ind. Fed'n of Dentists*, 476 U.S. 447, 459 (1986) (citations omitted).
- <sup>19</sup> *Eastman Kodak Co. v. Image Tech. Servs., Inc.*, 504 U.S. 451, 486–87 (1992) (Scalia, J., dissenting).
- <sup>20</sup> *National Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 691 (1978); see also *NCAA v. Bd. of Regents of the Univ. of Okla.*, 468 U.S. 85, 104 & n.26 (1984) ("[T]he essential inquiry remains the same—whether or not the challenged restraint enhances competition.").
- <sup>21</sup> While this article focuses on minimum RPM, it is worth noting that there have been no cases since *Khan* challenging maximum resale price maintenance agreements. Further, following the Supreme Court's *GTE Sylvania* decision, defendants have won a nearly uninterrupted string of victories in cases challenging territorial restrictions, virtually all at the motion to dismiss or summary judgment stage. The result has been that a whole category of antitrust litigation, previously robust, has virtually disappeared. As noted in the latest edition of the ABA's antitrust treatise, *Antitrust Law Developments*: "Most post-*Sylvania* decisions have upheld vertical territorial and customer restrictions under the rule of reason, even if imposed by a manufacturer with a dominant market position. In a few cases, courts have found territorial and customer restrictions unreasonable, though no court has done so in the last 25 years." ABA SECTION OF ANTITRUST LAW, ANTITRUST LAW DEVELOPMENTS 159 (7th ed. 2012) [hereinafter ALD].
- <sup>22</sup> 11 Civ. 6353CM, 2012 U.S. Dist. LEXIS 86628, at \*4, \*25, \*33–34 (S.D.N.Y. June 20, 2012).
- <sup>23</sup> See also *New York v. Tempur-Pedic Int'l, Inc.*, 916 N.Y.S.2d 900, 908–09 (N.Y. Sup. Ct. 2011). (dismissal for failure to prove agreement), *aff'd*, 944 N.Y.S.2d 518, 519 (2012); see, e.g., *Bel Canto Design*, 2012 U.S. Dist. LEXIS 86628; *Jacobs v. Tempur-Pedic Int'l, Inc.*, 626 F.3d 1327 (11th Cir. 2010) (affirming dismissal for failure to allege a valid product market); *PSKS, Inc. v. Leegin Creative Leather Prods., Inc.*, 615 F.3d 412 (5th Cir. 2010) (affirming dismissal of amended complaint following remand from the Supreme Court), *cert. denied*, 131 S. Ct. 1476 (2011).
- <sup>24</sup> *PSKS, Inc. v. Leegin Creative Leather Prods., Inc.*, 615 F.3d 412, 419 (5th Cir. 2010).
- <sup>25</sup> *FTC No. C-3937*, 2008 WL 2061410 (May 6, 2008).
- <sup>26</sup> ALD, *supra* note 21, at 80.
- <sup>27</sup> *Carrier, The Real Rule of Reason: Bridging the Disconnect*, 1999 B.Y.U. L. REV. 1265 (1999).
- <sup>28</sup> *Id.* at 1267–68.
- <sup>29</sup> *Id.* at 1346.
- <sup>30</sup> Michael A. Carrier, *The Rule of Reason: An Empirical Update for the 21st Century*, 16 GEO. MASON L. REV. 827, 829 (2009).
- <sup>31</sup> See *United States v. Visa U.S.A., Inc.*, 344 F.3d 229 (2d Cir. 2003).
- <sup>32</sup> *Carrier, supra* note 26, at 1348–49.
- <sup>33</sup> *Id.* at 1347.
- <sup>34</sup> *Id.* at 1275.
- <sup>35</sup> See, e.g., *Jacobs v. Tempur-Pedic Int'l, Inc.*, 626 F.3d 1327, 1339–40 (11th Cir. 2010) (complaint is "bereft of the critical allegations linking TPX's market power to harm to competition").
- <sup>36</sup> See, e.g., *Bel Canto Design*, 2012 U.S. Dist. LEXIS 86628.
- <sup>37</sup> See, e.g., *Spahr v. Leegin Creative Leather Prods., Inc.*, No. 2:07-CV-187, 2008 WL 3914461, at \*12 (E.D. Tenn. Aug. 20, 2008) (no allegation that "retailers have agreed to fix prices and then compelled the manufacturer, Leegin, to utilize resale price maintenance").
- <sup>38</sup> See, e.g., *Toledo Mack Sales & Serv. v. Mack Trucks, Inc.*, 530 F.3d 204, 225 (3d Cir. 2008) (involving evidence "that the restraint facilitates a retailer cartel") (citation and internal quotation marks omitted); *McDonough v. Toys "R" Us*, 638 F. Supp. 2d 461 (E.D. Pa. 2009); *BabyAge.Com, Inc. v. Toys "R" Us*, 558 F. Supp. 2d 575 (E.D. Pa. 2008) (motion to dismiss denied based on claims RPM was at behest of dominant retailer).
- <sup>39</sup> Gregory J. Werden, Senior Economic Counsel, Antitrust Division, U.S. Dep't of Justice, *Antitrust's Rule of Reason: Only Competition Matters* 16–28 (2013) (unpublished manuscript), available at SSRN: <http://ssrn.com/abstract=2227097> (forthcoming in 79 ANTITRUST L.J. (2014)). The paper expresses Werden's views and not necessarily those of the Department of Justice.
- <sup>40</sup> *Id.* at p. 21 (quoting *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 768 (1984)).
- <sup>41</sup> *Id.* at 22 (footnote omitted).
- <sup>42</sup> *Id.* at 24.
- <sup>43</sup> *Id.* at 26–27.
- <sup>44</sup> See, e.g., Maurice E. Stucke, *Does the Rule of Reason Violate the Rule of Law*, 42 U.C. DAVIS L. REV. 1375, 1485–87 (2009); Thomas A. Lambert, Dr. Miles Is Dead. Now What?: Structuring a Rule of Reason for Evaluating Minimum Resale Price Maintenance, 50 WM. & MARY L. REV. 1937, 1997–2005 (2009); Christine A. Varney, *A Post-Leegin Approach to Resale Price Maintenance Using a Structured Rule of Reason*, ANTITRUST, Fall 2009 at 22.
- <sup>45</sup> See, e.g., *Care Heating & Cooling, Inc. v. Am. Standard, Inc.*, 427 F.3d 1008, 1012 (6th Cir. 2005); *CDC Techs., Inc. v. IDEXX Labs., Inc.* 186 F.3d 74, 80 (2d Cir. 1999).
- <sup>46</sup> ALD, *supra* note 21, at 80 (footnotes omitted).
- <sup>47</sup> 11 HERBERT HOVENKAMP, ANTITRUST LAW ¶ 1912i, at 371 (3d ed. 2011). See also U.S. Dep't of Justice & Fed. Trade Comm'n Antitrust Guidelines for Collaborations Among Competitors (Apr. 2000), available at <http://www.ftc.gov/os/2000/04/ftcdojguidelines.pdf> (noting at sec. 3.37 in the context of rule-of-reason analysis of horizontal restraints that "The Agencies' comparison of cognizable efficiencies and anticompetitive harms is necessarily an approximate judgment."); see also Thomas A. Lambert, Dr. Miles Is Dead. Now What?: Structuring a Rule of Reason for Evaluating Minimum Resale Price Maintenance, 50 WM. & MARY LAW REV. 1937, 1962 (2009) ("The fact-finder thus would have to decide whether the post-RPM outcome of higher prices with more or better services is more or less desirable than the pre-RPM outcome of lower prices with fewer or inferior services. Absent some entirely arbitrary presumption that a low price is better than a high level of service (or vice versa), there is simply no way to make that decision.")
- <sup>48</sup> See, e.g., *PSKS*, 615 F.3d at 419 ("One problem with that argument [that RPM forecloses "free and open competition"] is that it ignores interbrand competition, which forces Brighton retailers to offer a combination of price and services that attracts consumers away from competing products.") The presence of robust interbrand competition also answers the concern raised by Professors Comanor and Scherer for the plight of the so-called inframarginal consumer—the shopper who values low price only and has no interest in receiving product education or other retailer-supplied services. See William B. Comanor, *Vertical Price Fixing, Vertical Market Restrictions and the New Antitrust Policy*, 98 HARV. L. REV. 983 (1985); Frederic M. Scherer, *The Economics of Vertical Restraints*, 52 ANTITRUST L. J. 687 (1983). In markets characterized by vibrant interbrand competition, these picky consumers should be able to find the low-price-no-services alternatives they prefer. See also Voorhees, *PEAs, PILs and MFNs*, ANTITRUST, Spring 2013 at 3.
- <sup>49</sup> *Id.* ("[The plaintiff] also fails to recognize that retailers will cease carrying Brighton goods if Leegin imposes onerous requirements that make Brighton products difficult to sell.")
- <sup>50</sup> *Federation of Dentists*, 476 U.S. at 459.
- <sup>51</sup> *Actavis*, 133 S. Ct. at 2238.
- <sup>52</sup> *Bel Canto Design*, 133 S. Ct. 2012 U.S. Dist. LEXIS 86628.