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Antitrust and Trade Regulation Update:

Vertical Price Fixing No Longer *Per Se* Unlawful

In a controversial 5-to-4 decision, the United States Supreme Court swept aside nearly a century of established antitrust precedent and held that vertical price fixing will no longer be deemed *per se* unlawful.

In *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, No. 06-480, decided June 28, 2007, the Court concluded that an agreement between a manufacturer and its dealers establishing resale prices should now be judged under what is known as the Rule of Reason. Under that approach, a dealer wishing to challenge a resale price agreement must show that the agreement's purpose and effect is not only anticompetitive but also outweighs any procompetitive benefits to interbrand competition.

The Court overturned its 96-year old precedent, *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911), which prohibited manufacturers from requiring retailers to agree to adhere to minimum resale prices. (Ten years ago, in *State Oil Company v. Khan*, the Court held that vertical maximum price fixing should be judged under the Rule of Reason, but had left in place the *per se* rule for minimum resale prices.)

Manufacturers should not assume, however, that they have *carte blanche* to impose minimum resale prices. Unless and until state courts or legislatures decide otherwise, resale price maintenance is still unlawful *per se* under many state antitrust laws, and state attorneys general have actively worked together to bring class actions challenging such arrangements. Moreover, even under the Rule of Reason, vertical price fixing may be risky in concentrated markets. And it is possible that the Federal Trade Commission may interpret Section 5 of the FTC Act to prohibit RPM as an unfair act or practice or an unfair method of competition.

Writing for the majority in the *Leegin* case, Justice Anthony Kennedy called the Court's earlier decision in *Dr. Miles* "a flawed antitrust doctrine that serves the interests of lawyers." He asserted that the older rule required "manufacturers to choose second-best options to achieve sound business objectives."

Consumer advocates immediately decried the *Leegin* ruling, asserting that allowing minimum price floors would hurt upstart discounters and Internet resellers seeking to offer new, cheaper ways to distribute products. The four dissenting justices agreed that the holding will drive up retail prices. "The only safe predictions to make about today's decision," Justice Breyer wrote in dissent, "are that it will likely raise the price of goods at retail and that it will create considerable legal turbulence."

As a practical matter, the Court's decision should give manufacturers of non-commodity and luxury goods more control over the resale prices of their products. While some believe that the *Leegin* ruling will not cause price increases at large discount retailers (because of their purchasing power over manufacturers), the case will make it harder for smaller boutiques that offer specialty or customized goods to discount prices without the manufacturer's approval.

The ruling in *Leegin* surprised many who expected the Court to defer making such a major change in antitrust law to Congress in light of the many court decisions by the Supreme Court and other courts applying the *per se* rule over the years as well as Congress' own action favoring the *per se* rule against resale price maintenance when it repealed the fair trade laws in 1975.

Justice Kennedy dismissed this concern, saying that the principle that past decisions should be left alone "does not compel our continued adherence" in this instance because the economics literature suggest that the long-standing decision "is inappropriate, and there is now widespread agreement" that price floors can help promote competition.

The dissenting Justices argued that changes in the economy since 1975, including the increasing concentration in the retail sector, actually strengthened the case for the *per se* rule.

The case arose from a dispute over the resale price of designer handbags made by Leegin, which makes the Brighton line of purses. Leegin required its retailers, including plaintiff Kay's Kloset, to agree in writing not to sell Leegin products below certain prices. When Kay's Kloset sold at lower prices and was terminated by Leegin, it filed suit in 2002 and won a jury verdict of \$3.6 million in damages.

On appeal, Leegin argued that it needed to maintain price consistency among the niche retailers it sells to in order to ensure that the stores can and will offer high quality customer service. This would enable smaller stores to compete against rival brands sold by discounters, the manufacturer argued.

The case has been remanded to the lower courts for further proceedings.

To discuss the application of the *Leegin* decision to your company's pricing program or policies or for further information about recent antitrust decisions of the Supreme Court, contact a member of Schiff Hardin's antitrust practice group.

For Further Information

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