FEDERAL TRADE COMMISSION

RESALE PRICE MAINTENANCE WORKSHOP - P090400

Submission of:

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I. Introduction

This submission addresses the Federal Trade Commission's request for comment regarding the legal doctrines and jurisprudence related to resale price maintenance by examining an issue that all national manufacturers conducting business in a post-*Leegin* world must confront, i.e., the continued application of the per se rule invalidating minimum resale price maintenance agreements by the several States. This issue is fundamentally important to the successful practical implementation of the Supreme Court's *Leegin* decision. As explained more fully below, the policies of the Sherman Act, as enunciated in *Leegin*, will be frustrated unless state laws condemning minimum resale price maintenance as per se unlawful are preempted or precluded by federal law.

II. State Antitrust Law as an Obstacle to the Accomplishment of the Purposes of Federal Antitrust Law for the Sale of Goods

One of the fundamental precepts of constitutional law is the supremacy of federal law over state law and the concomitant doctrine of preemption. Federal law can preempt state law in one of three ways: (1) Congress can expressly preempt state law; (2) federal law can "occupy the field"; or (3) there can be a conflict between state law and federal law. This third possibility – conflict preemption – can arise either "where it is impossible for a private party to comply with

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both state and federal law" or "where 'under the circumstances of [a] particular case, [the challenged state law] stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.'" *Crosby v. Nat'l Foreign Trade Council*, 530 U.S. 363, 372-73 (2000) (quoting *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941)). The application of state antitrust law to minimum resale price maintenance agreements after the Supreme Court's decision in *Leegin* implicates this latter form of conflict preemption: state antitrust law stands as an obstacle to the accomplishment and execution of the Sherman Act's purposes.

The purposes of the Sherman Act are well-known and undisputed. Over fifty years ago, the Supreme Court held that

> [t]he Sherman Act was designed to be a comprehensive charter of economic liberty aimed at preserving free and unfettered competition as the rule of trade. It rests on the premise that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress, while at the same time providing an environment conducive to the preservation of our democratic political and social institutions. But even were that premise open to question, the policy unequivocally laid down by the Act is competition.

Northern Pacific R. Co. v. United States, 356 U.S. 1, 4-5 (1958). Rather than effectuating this purpose via meticulously-written legislation, however, the Sherman Act actually cedes power from the Legislative to Judicial Branch, as its goals are fulfilled through the common law tradition. *See Leegin Creative Leather Products v. PSKS, Inc.*, 127 S. Ct. 2705, 2714 (2007) ("[T]he Sherman Act's use of 'restraint of trade' 'invokes the common law itself, . . . not merely the static content that the common law had assigned to the term in 1890.'" (quoting *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717, 732 (1988)). Congress's decision to develop antitrust law through the courts was purposeful. This method enables the law to adapt to changing economic understandings and, indeed, the *Leegin* decision could not be a more perfect illustration of this tradition.

In *Leegin*, the Supreme Court held that the per se rule is not appropriate for resale price maintenance because it is not a restraint that "'would always or almost always tend to restrict competition and decrease output.'" *Leegin*, 127 S. Ct. at 2713 (quoting *Business Electronics Corp.*, 485 U.S. at 723). Much to the contrary, the Court found that minimum resale price maintenance agreements have many tangible procompetitive benefits.

Specifically, the Court found that minimum resale price maintenance eliminates intrabrand price competition which, "in turn[,] encourages retailers to invest in tangible or intangible services or promotional efforts that aid the manufacturer's position as against rival manufacturers." *Leegin*, 127 S. Ct. at 2715. Similarly, "[r]esale 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." *Id.* In addition, the Court recognized that a procompetitive benefit of minimum resale price maintenance is the curtailment of free riders. *See id.* at 2716 ("Minimum resale price maintenance alleviates the [free riding] problem because it prevents the discounter from undercutting the service provider. With price competition decreased, the manufacturer's retailers compete among themselves over services.").[2] Further, "[r]esale price maintenance . . . can increase interbrand competition by facilitating market entry for new firms and brands[]" – a particularly important benefit because "[n]ew products and new brands are essential to a dynamic economy, and if markets can be penetrated by using resale price maintenance there is a procompetitive effect." *Id.*

[2] In fact, the Court recognized that "[r]esale price maintenance can also increase interbrand competition by encouraging retailer services that would not be provided even absent free riding." *Id.* This is the case because "[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[,]" but "[o]ffering 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." *Leegin*, 127 S. Ct. at 2715.

If states continue to apply the per se rule to these agreements, the above procompetitive benefits to minimum resale price maintenance cannot be realized. This "increase[s] the total cost of the antitrust system by prohibiting procompetitive conduct the antitrust laws should encourage." *Leegin*, 127 S. Ct. at 2718. *Leegin*, and the federal antitrust regime as a whole, loses its relevancy if manufacturers cannot experiment with minimum resale price maintenance agreements for fear of state prosecution under the per se rule. Yet, the conduct and commentary of state enforcers since *Leegin* suggests that this is precisely what the states plan to do.

III. Per Se Condemnation of Resale Price Maintenance by the Several States

Since *Leegin* was decided in June 2007, commentators have predicted that states would continue to apply the per se rule to minimum resale price maintenance under their own antitrust statutes. *See* Michael A. Lindsay, *Resale Price Maintenance and the World After* Leegin, ANTITRUST MAGAZINE, Vol. 22, No. 1 at 33 (Fall 2007) ("[S]ince *Leegin* did not hold minimum RPM agreements per se legal, state and private enforcers can be expected to argue that contrary state laws are not preempted."); Joel M. Mitnick, et al., *On Life Support from* Leegin*aire's Disease: Can the States Resuscitate* Dr. Miles?, ANTITRUST MAGAZINE, Vol. 22, No. 3 at 67 (Summer 2008) ("[S]tate antitrust enforcers are likely to argue that RPM constitutes a per se violation of pre-existing state antitrust laws[.]"). While some states' antitrust laws mirror the Sherman Act's brevity, *see e.g.*, FLA. STAT. § 542.18 (2007); WASH. REV. CODE § 19.86.030 (2007), other states specify that certain conduct, such as price fixing (without distinguishing vertical from horizontal) is per se illegal, *see e.g.*, 740 ILL. COMP. STAT. 10/3(1)(a) (2007); HAW. REV. STAT. § 480-4(b)(1) (2007). These latter states are likely to rely on these statutes and take the position that their state law is differentiated from, and therefore not bound by, federal antitrust law. But, even the former states appear prone to apply a per se rule, and take the

position that their "little Sherman Act section 1s" should be interpreted differently than the federal counterpart.

Indeed, some state enforcers have made their intentions to continue the per se regime clear: "The history of the fair trade laws, the repeal of the fair trade laws, and the enactment of section 369-a illustrate precisely the differences that justify concluding that New York law prohibits vertical price fixing, despite *Leegin*." Robert L. Hubbard, *Protecting Consumers Post-Leegin*, ANTITRUST MAGAZINE, Vol. 22, No. 1 at 43 (Fall 2007). *See also* Mitnick, *supra* at 63 ("[E]nforcement officials of several states have asserted that RPM remains per se unlawful under various state antitrust laws despite *Leegin*.").[3]

True to the enforcers' word – and rendering the commentators' statements prescient – a complaint filed in March of 2008 suggests that New York, along with two other states, continue to apply the per se rules to minimum resale price maintenance.

On March 25, 2008, the States of New York, Illinois and Michigan entered into a Stipulated Final Judgment and Consent Decree ("Consent Decree") with Herman Miller, Inc. *See State of New York, et al. v. Herman Miller, Inc.*, No. 08-cv-2977 (S.D.N.Y. March 25, 2008) [Docket No. 2]. The Consent Decree was "based on an investigation conducted by the States of New York, Illinois, and Michigan (the 'Plaintiff States') into possible resale price maintenance and other antitrust violations by Herman Miller, Inc.'s ('Herman Miller') Herman Miller for the Home division ('HMH')[.]" Consent Decree at 1. The Complaint alleged that "HMH and several of its Dealers agreed to offer HMH Furniture to consumers at prices not below HMH's MSRP, and other conduct in violation of federal and state antitrust laws." *Id.* at 2. Although the three states did not explicitly allege that Herman Miller's conduct was a per se violation of New

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York, Illinois and Michigan antitrust law, there was no allegation that Herman Miller possessed market power in the relevant market of "high-end ergonomically designed office chairs." *See State of New York, et al. v. Herman Miller, Inc.*, No. 08-cv-2977 (S.D.N.Y. March 21, 2008) [Docket No. 1]. This omission suggests that the states' theory was indeed based on a per se analysis.

Given the public discourse following *Leegin*, New York, Illinois and Michigan's action against Herman Miller was not unanticipated. It was, nevertheless, a tangible indication that the conflict between state and federal antitrust law is not merely hypothetical. Rather, this conflict represents a very real obstacle to the accomplishment of the procompetitive benefits to minimum resale price maintenance recognized in *Leegin*.

IV. State Antitrust Law Preemption for Professional Sports Leagues

In other markets where state antitrust law stands as an obstacle to, or places an impermissible burden on, the functioning of an interstate market, courts have either preempted state law or struck it down pursuant to dormant Commerce Clause principles. Oft-cited examples are cases involving Major League Baseball, the National Basketball Association and the National Football League.

The seminal professional-sports-league case is *Flood v. Kuhn*, 443 F.2d 264 (2d Cir. 1971), *aff'd* 407 U.S. 258 (1972). In language that is just as applicable to the sale of goods in today's national, on-line economy as it was to the rules governing transactions in professional sports leagues, the Second Circuit held that "where the nature of an enterprise is such that differing state regulation, although not conflicting, requires the enterprise to comply with the strictest standard of several states in order to continue an interstate business extending over many states, the extra-territorial effect which the application of a particular state law would exact constitutes, absent a strong state interest, an impermissible burden on interstate commerce."

Flood, 443 F.2d at 267 (citing *Southern Pacific Co. v. Arizona*, 325 U.S. 761, 774-75 (1945)). The *Flood* court did not find a strong state interest in antitrust regulation, and consequently precluded application of state antitrust law. *See* 443 F.2d at 268 ("On the one hand, it is apparent that each league extends over many states, and that, if state regulation were permissible, the internal structure of the leagues would require compliance with the strictest state antitrust standard. . . . On the other hand, we do not find that a state's interest in antitrust regulation, when compared with its interest in health and safety regulation, is of particular urgency.").

The Supreme Court affirmed. It was unclear, however, whether the Supreme Court's holding was based on the Second Circuit's dormant Commerce Clause analysis, or the earlier decision of the district court which was based on preemption. The Supreme Court first observed that the district court "rejected the state law claims because state antitrust regulation would conflict with federal policy and because national 'uniformity (is required) in any regulation of baseball and its reserved system.'" *Flood v. Kuhn*, 407 U.S. at 284 (quoting *Flood v. Kuhn*, 316 F. Supp. 271, 280 (S.D.N.Y. 1970)). But the Court then observed that "[t]he Court of Appeals, in affirming, stated, '(A)s the burden on interstate commerce outweighs the states' interests in regulating baseball's reserve system, the Commerce Clause precludes the application here of state antitrust law.'" *Flood*, 407 U.S. at 284 (quoting *Flood*, 443 F.2d at 268). Rather than explain whether the Court was persuaded by either preemption, the dormant Commerce Clause balancing test, or both, the opinion merely stated that ***"these statements adequately dispose of the state law claims."*** *Flood*, 407 U.S. at 284-85 (emphasis added).

Recognizing that the Court's *Flood* opinion was "somewhat ambiguous," courts have interpreted it as "approving both bases [preemption and dormant Commerce Clause] for the lower courts' rejection of Flood's state law claims." *Robertson v. Nat'l Basketball Ass'n*, 389 F.

Supp. 867, 880 (S.D.N.Y. 1975). In a particularly clearly-written opinion, the Eleventh Circuit agreed with *Robertson*, stating that "[a] careful reading of the passage yields ***two*** different theories. . . . [T]he district court advanced a preemption theory . . . [and] [t]he Second Circuit Court of Appeals, by contrast, relied upon the Commerce Clause." *Major League Baseball v. Crist*, 331 F.3d 1177, 1185 (11th Cir. 2003). Both rationales were applicable to professional sports leagues, and both are relevant to the sale of goods in the national economy.

Of course, as discussed in *Flood*, *Crist* and other professional-sports-league cases, baseball does enjoy unique status in antitrust jurisprudence. *See generally Flood*, 443 F.2d at 265-66. But the preemption of state antitrust law to baseball is not based on this unique status. Rather, courts have held that state antitrust law is preempted when the transaction at issue involves other professional sports leagues that do not enjoy the same federal antitrust exemption. *See Robertson*, 389 F. Supp. at 880-81; *Partee v. San Diego Chargers Football Co.*, 34 Cal. 3d 378 (1983). For example, in *Partee*, the California Supreme Court held that the Cartwright Act was inapplicable to professional football. *Partee* based its decision, as did *Flood*, on both preemption and dormant Commerce Clause grounds. 34 Cal. 3d at 385. Specifically, the Court held that the "national uniformity required in regulation of baseball and its reserve system is likewise required in the player-team-league relationships challenged by Partee ***and*** . . . the burden on interstate commerce outweighs the state interests in applying state antitrust laws to those relationships." *Id.* (emphasis added). Moreover, the Court flatly rejected Partee's argument that the inapplicability of state antitrust law to baseball was based on its unique exemption from federal antitrust law. *See id.* Rather, whenever (1) an industry requires uniformity or (2) the burden on interstate commerce from state antitrust regulation outweighs the

state's competing interest, state antitrust law will not apply. *See id.* This was true for other professional sports leagues, and it is true for the sale of goods in today's economy.

In fact, if state antitrust law is preempted based on the "dubious rationales" supporting baseball's antitrust exemption, *see Crist*, 331 F.3d at 1188 ("The exemption was founded upon a dubious premise, and it has been upheld in subsequent cases because of an equally dubious premise."), then it follows, *a fortiori*, that state law should be preempted for manufacturers engaging in minimum resale price maintenance following *Leegin*'s unequivocal holding. Thus, applying *Flood*, *Crist*, *Robertson* and *Partee*, courts are likely to find state antitrust law inapplicable to minimum resale pricing agreements under either the doctrine of preemption, the dormant Commerce Clause, or both.

V. *ARC America*

The several states will undoubtedly dispute the inapplicability of state antitrust law by citing to *California v. ARC America Corp.*, 490 U.S. 93 (1989). Indeed, one state enforcer has already relied on this case for the proposition that "[s]tate law is wholly enforceable even if it diverges from federal antitrust jurisprudence on vertical price fixing." Robert L. Hubbard, *supra* at 43. And, furthermore, at least one neutral commentator has observed that "the Supreme Court has made clear that state antitrust law is not preempted even when the state statute or state judicial or agency interpretations are inconsistent with prevailing federal law." Herbert Hovenkamp, *Antitrust Law* ¶ 2403a at 318 (2006). A close look at *ARC America*, however, indicates that this ostensibly "clear" statement of law does not necessarily follow from the case itself.

In *ARC America*, a number of states sought to recover from cement companies for an alleged horizontal price fixing conspiracy. The states were, at least in part, indirect purchasers of the concrete and therefore, pursuant to *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), could

not recover under the federal antitrust laws. Recognizing this limitation in federal law, these states brought both federal and state antitrust claims. *ARC America*, 490 U.S. at 98. Thus, the issue before the Court was "whether th[e] rule limiting recoveries under the Sherman Act also prevents indirect purchasers from recovering damages flowing from violations of state law, despite express state statutory provisions giving such purchasers a damages cause of action." *Id.* at 100. The Court answered this question in the negative.

ARC America, however, dealt only with the question whether, assuming liability was pre-determined, a certain group of plaintiffs could recover under state law when that same group could not recover under federal law. That issue is fundamentally distinct from the question whether a party can be liable for a price fixing conspiracy under state law yet not liable for the same conduct under federal law, and this distinction has not been lost on other commentators. *See* Lindsay, *supra* at 33 ("*ARC America* dealt with a procedural or remedial rule, rather than a substantive rule of conduct. *Leegin*, however, dealt with a substantive rule of conduct: whether minimum RPM agreements are automatically illegal.").[4] The latter question – *i.e.,* whether state law can apply where it condemns conduct that federal law permits – is squarely presented by *Leegin* and the states' adherence to the former per se regime. The question of ***liability*** under one regime but not the other was neither addressed nor decided in *ARC America.*

[4] Indeed, the distinction between remedy and liability is not only apparent from the *ARC America* decision itself, but from the cases upon which it relies: *Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238 (1984) and *California v. Zook*, 336 U.S. 725 (1949). In *Silkwood*, the plaintiff's decedent was injured as a result of nuclear contamination. State tort law permitted punitive damages for these types of injuries (if the jury found certain facts), but there was no such remedy under the federal Atomic Energy Act. The court held that the plaintiff could recover punitive damages under state law even though that remedy was not available under federal law. In *Zook*, the Supreme Court held that California's criminal law could be applied to share-expense passenger transport even though federal criminal law covered the same subject-matter. The Court's decision was based on the fact that the California and federal laws were consistent, specifically noting that "[t]he case would be different if there were conflict in the provisions of the federal and California statutes." *Zook*, 336 U.S. at 735.

V. Conclusion

In *Leegin*, the Court detailed the many procompetitive benefits of minimum resale price maintenance agreements. Encouraging firms to engage in competition-enhancing and consumer-benefiting activities is, just as much as deterring anticompetitive conduct, central to the purposes for which the Sherman Act was passed. Some of the states have expressed – and now shown – their willingness to condemn all minimum resale price maintenance agreements in the name of their own antitrust laws. This continued adherence to the former per se regime constitutes an obstacle to the effectuation of the purposes of the Sherman Act. As such, and following the lead of the professional sports league cases, the states should be precluded from stifling the progress of the Sherman Act either through the doctrine of preemption, dormant Commerce Clause principles, or both.

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