ANNOUNCING THE DEATH OF COLGATE: THE FORM AND SUBSTANCE OF VERTICAL PRICE FIXING AGREEMENTS

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ABSTRACT:

This Article examines the agreement requirement in resale price maintenance ("RPM") cases and the longstanding exception to the ban on RPM under the *Colgate* doctrine. It argues for the abolition of the doctrine for a number of reasons. First, there are no persuasive theoretical justifications for requiring an agreement in RPM cases as the most relevant purpose served by an agreement requirement under antitrust law does not apply to RPM. Second, there is no logically coherent and theoretically sound theory of agreement under the doctrine, which means that there is no principled way to apply the agreement concept in RPM cases. Third, there is no sound economic basis for requiring an agreement in RPM cases as none of the main theories of harm and pro-competitive justifications of RPM is premised on an agreement. Finally, it is argued that the *Colgate* doctrine has provided a highly unsatisfactory safe harbor for businesses to implement RPM due to costs and manpower involved in complying with the jurisprudence under *Colgate*. This Article also argues that dealer termination requires a different treatment from that accorded by *Monsanto* and *Business Electronics* after *Leegin* and proposes a framework for determining the legality of dealer termination independent of the existence of an RPM scheme.

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INTRODUCTION

The *Colgate* doctrine and the associated issue of an agreement requirement for resale price maintenance ("RPM") schemes have long been a source of confusion and needless complication in antitrust analysis. The *Colgate* doctrine holds that it is permissible for a supplier to implement an RPM scheme through unilateral policy announcements and a refusal to deal with non-compliant dealers. The doctrine draws a line between permissible unilateral conduct and illegal concerted action. The doctrine itself is simple enough to understand. Its application, however, has been beset with difficulties. The Supreme Court spent a great part of the last century attempting to clarify the precise scope of the doctrine. In the process, it has implicitly proposed a number of theories of agreement to help the courts decide when an illegal agreement is consummated. Unfortunately, none of these theories are logically coherent or theoretically sound, nor do they provide meaningful guidance to businesses. More fundamentally, the insistence on an agreement in the RPM context is much ado about nothing. The purpose of an agreement requirement is to help us identify conduct with possible anticompetitive effects. For RPM, regardless of the existence of an agreement, the fact that the dealers comply with the supplier's demand of minimum resale prices means that resale prices are maintained. The agreement requirement is completely divorced from the economic effects of RPM. None of the main theories of harm and economic justifications for RPM are premised on an agreement. The harm and benefits will materialize as long as resale prices are maintained, either through unilateral compliance or a mutual agreement. The *Colgate* doctrine and the subsequent efforts to distinguish between permissible unilateral conduct and illegal concerted action have rendered compliance with the law on RPM needlessly costly and complex. The only beneficiaries of this state of affairs are lawyers advising clients.

There would have been stronger justifications for these inefficiencies if the *per se* rule for RPM were still in place. Under the *per se* rule, some clearly competitively harmless conduct was condemned. Efforts were made to use the agreement requirement to carve out such conduct. Using a formal device such as an agreement requirement to tackle a substantive issue is ineffective at best. Unfortunately, that was the only available solution when the *per se* rule applied. This is no longer the case after *Leegin*. With the abolition of the *per se* rule, all the previous justifications for maintaining the agreement requirement have disappeared. It is, therefore, worth taking a hard look at the continual validity of the *Colgate* doctrine and the agreement requirement.

This Article thus follows Professor Kaplow's lead in critiquing the continual relevance of the vertical agreement requirement in antitrust analysis.[1] However, it differs from Kaplow's analysis in a number of important ways. First, it is only concerned with the agreement requirement in resale price maintenance cases rather than vertical agreements in general. In particular, it focuses on the theoretical underpinning and continual viability of the *Colgate* doctrine. Second, it provides a much more detailed overview of the case law and delves more closely into the logical inconsistencies in *Monsanto* and *Business Electronics*, two of the most recent Supreme Court cases on the vertical agreement issue. Third, while

1. Louis Kaplow, *The Meaning of Vertical Agreement and the Structure of Competition Law*, 80 ANTITRUST L.J. 563, 563 (2016).

Kaplow stops short of arguing for the abolition of the vertical agreement requirement outright, this Article proposes the abrogation of the *Colgate* doctrine to achieve greater clarity and logical consistency in the law. However, much of the logic in Kaplow's arguments would be equally relevant here.

This Article is divided into eight sections. After this introduction, Section II provides an overview of the Supreme Court jurisprudence on the *Colgate* doctrine and the agreement requirement for RPM. Section III examines the various possible purposes for requiring the proof of an agreement under antitrust law and questions whether the relevant purpose applies to the RPM context. Section IV explores the various theories that have been put forward in the case law on the notion of an agreement and assesses their logical coherence and theoretical soundness. Section V discusses the prevailing economic theories of harm and justifications for RPM and concludes that none of them is premised on the existence of an agreement. Section VI reviews the practical justification for the *Colgate* doctrine and argues that the doctrine has done more harm than good from a business perspective. Section VII summarizes the various proposals put forward in this Article and explains how they should be applied. Section VIII concludes the Article.

I. EVOLUTION OF THE CASE LAW ON THE NOTION OF AGREEMENT IN VERTICAL RESTRAINTS

The notion of a vertical agreement in the context of RPM has long puzzled the courts. An agreement is required in order to establish a violation of Section 1 of the Sherman Act. Determining the existence of an agreement between the supplier and the dealers in the context of an RPM is not always a straightforward issue. In *United States v. Colgate & Co.*, the Supreme Court promulgated the *Colgate* doctrine, which held that a supplier has the right to announce the conditions upon which it will deal with suppliers and to refuse to deal with those who fail to abide by the conditions.[2] The case laid down the simple, and seemingly uncontroversial, rule that unilateral imposition of an RPM does not violate Section 1.[3] The devil, however, is in the details. What followed in the ensuing decades was a string of cases in which the Supreme Court attempted to determine what conduct qualifies as permissible unilateral conduct and what constitutes an illegal concerted action between the supplier and the dealers in a variety of factual scenarios.

2. United States v. Colgate & Co., 250 U.S. 300, 307 (1919).
3. *Id.*

A. *Colgate and Its Progeny*

1. United States v. Colgate & Co.

After laying down the *per se* rule for RPM in *Dr. Miles*[4], the Supreme Court was again confronted with an RPM case in *United States v. Colgate & Co*. At issue was whether the conduct perpetrated by Colgate in the case constituted an RPM illegal *per se* under *Dr. Miles*.[5] In language that has been repeatedly quoted by the courts ever since, Justice McReynolds held that Colgate's course of conduct in the case constituted permissible unilateral conduct under Section 1, declaring that:

> In the absence of any purpose to create or maintain a monopoly, the act does not restrict the long recognized right of trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal; and of course, he may announce in advance the circumstances under which he will refuse to sell.[6]

This has come to be known as the *Colgate* doctrine.

There was some confusion as to the basis upon which the Court proclaimed the *Colgate* doctrine. The confusion stems from the fact that while the trial court judge interpreted the indictment in the case as alleging no agreement and nothing more than unilateral conduct,[7] the factual record suggested that Colgate went substantially beyond that.[8] This confusion has led commentators to question the foundation of the doctrine.[9] Other commentators have questioned the precise scope of the doctrine. Hay

4. Dr. Miles Med. Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911).

5. *Colgate*, 250 U.S. at 306.

6. *Id.* at 307.

7. *Id.* at 304.

8. The factual record indicated that Colgate "requests, often complied with, information concerning dealers who had departed from specified prices; investigat[es] . . . those not adhering thereto and plac[es] their names upon 'suspended lists;' requests to offending dealers for assurances and promises of future adherence to prices, which were often given . . . ." *Id.* at 303. This anomaly is due to the Criminal Appeals Act, under which the Supreme Court had no authority to review the interpretation of an indictment by a lower court and instead must confine itself to the question of whether the lower misconstrued the statute. *Id.* at 301-02.

9. Edward H. Levi, *The Parke, Davis-Colgate Doctrine: The Ban on Resale Price Maintenance*, SUP. CT. REV. 258, 285-92 (1960) (arguing that Levi argues *Colgate* itself does not lend support to doctrine); Terry Calvani & Andrew G. Berg, *Resale Price Maintenance after Monsanto: A Doctrine Still at War with Itself*, DUKE L.J. 1163, 1169 (1984) ("The fact that the *Colgate* decision rested heavily on procedural aspects of the case—the government's failure to allege the existence of illegal agreements—made the Court's attempted distinction between unilateral action and concerted conduct of uncertain precedential value.").

observes that "[n]arrowly construed, *Colgate* merely holds that under [S]ection 1 of the Sherman Act a plaintiff must allege an agreement between the manufacturer and dealers."[10] Only if read more broadly did *Colgate* meaningfully limit the application of Section 1 to vertical restraints.[11]

2. United States v. A. Schrader's Son Inc.

The Supreme Court proceeded to address the question as to the precise scope of the *Colgate* doctrine in a series of cases in the next few decades. The Supreme Court encountered its first RPM case post-*Colgate* a year later in *United States v. A. Schrader's Son, Inc*.[12] The district court in this case had noted that the only difference it could discern between *Dr. Miles* and *Colgate* was the existence of written agreements in *Dr. Miles* and their absence in *Colgate*.[13] The district court concluded that that was a distinction without a difference, and therefore *Dr. Miles* must have rested on a different principle: that there is no violation of Section 1 absent a purpose to monopolize interstate trade.[14] In overruling the district court, the Supreme Court clarified that *Colgate* was not meant to overrule *Dr. Miles*, and reiterated the distinction between permissible unilateral action and an agreement to fix resale prices.[15] The Supreme Court further indicated that an agreement can be "implied from a course of dealing or other circumstances."[16] An agreement for RPM purposes need not be express, as in *Dr. Miles* and *Colgate*.

3. Frey & Son v. Cudahy Packing

A year later, the Supreme Court held in *Frey & Son v. Cudahy Packing* that there is no agreement for the purpose of Section 1 if the defendant merely announced a policy of refusal to sell to previously non-compliant dealers, repeatedly called its dealers' attention to the policy, and the dealers

10. George A. Hay, *Vertical Restraints After Monsanto*, 66 CORNELL L. REV. 418, 424 (1985).

11. *Id.*

12. United States v. A. Schrader's Son, Inc., 252 U.S. 85 (1920).

13. *Id.* at 97.

14. *Id.* at 97-98. Viewed from the perspective of subsequent cases, the district court's decision was befuddling in that it was undisputed that there were agreements between the defendant and its dealers in the case. The district court had noted that all of the defendant's contracts with the dealers provided that the dealers "should not resell such products at prices other than those fixed by the defendant." *Id.* at 95. The case clearly falls on the side of *Dr. Miles* in the *Dr. Miles-Colgate* divide.

15. *Id.* at 99.

16. *Id.*

quietly acquiesced to the policy and abided by it.[17] *Cudahy Packing* was to be the only case in which the Supreme Court would rule in favor of the defendant in an RPM case where the existence of an agreement was at issue until the 1980s. The Court reiterated the fact that an agreement can be implied from course of conduct and circumstances. By so holding, however, the Court implicitly drew a distinction between an express agreement, albeit implied from circumstantial evidence, and tacit acquiescence.[18]

From the perspective of the *Colgate* doctrine, the most interesting part of the *Cudahy Packing* opinion was the dissent. Justice Pitney argued that the defendant and its dealers' course of conduct in the case provided a sufficient basis for a jury to infer the existence of an agreement.[19] Justice Pitney noted that:

> [U]pon finding many persons, actuated by a common motive, exchanging communications between themselves respecting a plan of conduct and acting in concert in precise accordance with the plan, the jury might find that they had agreed or combined to act as in fact they did act; that their simultaneous pursuit of an identical programme was not a miraculous coincidence, but was the result of an agreement or combination to act together for a common end.[20]

4. FTC v. Beech-Nut Packing

In *FTC v. Beech-Nut Packing*, the Supreme Court confronted for the first time the issue of the permissible amount of enforcement effort in a unilateral RPM policy.[21] The Court held that the defendant's conduct in the case had crossed the line of permissible unilateral conduct and constituted an agreement for the purpose of Section 1.[22] The opinion referred to a wide range of conduct. The Court, however, admonished the FTC to focus on four

17. Frey & Son v. Cudahy Packing, 256 U.S. 208, 209-10 (1921).

18. C. Douglas Floyd, *Vertical Antitrust Conspiracies After Monsanto and Russell Stover*, 33 U. KAN. L. REV. 269, 289 (1985).

19. *Cudahy Packing*, 256 U.S. at 216-17.

20. *Id.* at 217. Justice Pitney's exact position on the *Colgate* doctrine is unclear. On the one hand, his disagreement with the majority indicates that, in his view, the sort of unilateral conduct that is ostensibly exempted by the *Colgate* doctrine should constitute an agreement. On the other hand, his reference to the exchange of communication between the supplier and its dealers suggests that his view can be reconciled with the *Colgate* doctrine, which has been understood to prohibit direct and indirect communication between the supplier and its dealers. However, subsequent language in his dissent suggests that Justice Pitney did not consider exchange of communication to be necessary for finding an agreement. *Id.* at 217-18. Concerted action in pursuit of self-interests would suffice.

21. FTC v. Beech-Nut Packing, 257 U.S. 441 (1922).

22. *Id.* at 455.

types of conduct in its order. The enumerated conduct includes (1) reporting the names of offending dealers; (2) putting offending dealers on lists of no supply unless these dealers provide assurance that they will not sell below the stipulated prices again; (3) using salesmen and agents to monitor compliance by the dealers; and (4) using numbers and symbols to track the passage of products to ensure compliance with the RPM scheme.[23] Interestingly, the Court did not designate the defendant seeking assurances from jobbers and wholesale dealers of future compliance and securing the cooperation of wholesalers, jobbers, and retailers in reporting price cutters as conduct to be proscribed by the FTC's order.[24] Such conduct turned out to be crucial in subsequent cases. Explaining the reasons that the Court found the enumerated conduct objectionable, the Court noted that the system went "far beyond the simple refusal to sell goods to persons who will not sell at stated prices,"[25] and showed "suppression of the freedom of competition by methods in which the company secures the co-operation of its distributors and customers, which are quite as effectual as agreements express or implied intended to accomplish the same purpose."[26] What tipped the balance in the case was the comparable effectiveness of the ostensibly unilateral conduct in maintaining an RPM scheme.[27]

23. *Id.* at 456. Some commentators have emphasized other conduct in the case as particularly relevant, such as, "tracing price cutters, separating retailers from banned wholesalers, and requiring wholesalers not to sell to price-cutting retailers until (after assurances as to future conduct) they were restored." Levi, *supra* note 9, at 299-300.

24. However, some commentators have deemed the use of intermediaries to monitor compliance by retailers as a crucial fact in the case. *See, e.g.*, Herbert J. Hovenkamp, *Leegin, the Rule of Reason, and Vertical Agreement*, U. IOWA LEGAL STUDIES RESEARCH PAPER NO. 10-40 (2010), http://ssrn.com/abstract=1673519 [https://perma.cc/265V-4J6F] ("In *Beech-Nut*, involving traditional agreements and the use of intermediaries to control retailers, the Court emphasized the policy against resale price maintenance in finding a violation of Federal Trade Commission Act §5."); Glen O. Robinson, *Explaining Vertical Agreements: The Colgate Puzzle and Antitrust Method*, 80 VA. L. REV. 577, 584 (1994) ("In *FTC v. Beech-Nut Packing Co.*, it held that the requisite agreement could be found from a manufacturer's enlisting wholesalers actively to monitor retailers to ensure compliance.").

25. *Beech-Nut*, 257 U.S. at 454.

26. *Id.* at 455.

27. The dissent criticized the majority's determination of legality based on the mechanisms used to enforce the RPM scheme and the effectiveness of the mechanisms. *Id.* at 459. The dissent argued that if the defendant had the right to choose with whom it would deal, there would be no reasons to prohibit the defendant from recording the names of non-compliant dealers, using special salesmen to monitor compliance, or marking its products with number and symbols to allow easy tracing. *Id.* If the distinction was between unilateral conduct and concerted action, all three types of conduct would seem to be unilateral in nature because they do not involve joint action on the part of the defendant and the dealers. However, there is clearly conduct in the case that is not unilateral in nature, such as seeking assurances from wholesalers and jobbers of compliance and enlisting wholesalers and jobbers to monitor compliance by retailers.

5. U.S. v. Bausch & Lomb Optical

In *U.S. v. Bausch & Lomb Optical*, the focus was again on how the defendant enforced the RPM scheme.[28] The Supreme Court found that the conduct at issue exceeded permissible unilateral conduct on two grounds.[29] The first ground was that the wholesalers accepted the defendant's "plan of distribution by cooperating in prices, limitation of sales to and approval of retail licensees."[30] The Court did not specify how the wholesalers accepted the plan. Prior to noting their acceptance of the plan of distribution, the Court commented that "there is more here than mere acquiescence of wholesalers . . . ."[31] A review of the Court's description of the operation of the plan, however, suggests that the wholesalers did not expressly communicate their acceptance to the defendant.[32] They merely acted according to the wishes of the defendant. The second ground was an agreement between the defendant and some of the wholesalers to fix resale prices and to limit sales to retailers approved by the defendant.[33] Noteworthy is the Court's observation that whether the agreement was attained by an express agreement or "by acquiescence of the wholesalers coupled with assistance in effectuating its purpose is immaterial."[34] In other words, it seems that on both grounds, it would have sufficed if the wholesalers merely acquiesced to the defendant's demands without any explicit communication.[35] This creates the anomalous situation where there is no agreement if the retailers comply with the supplier's conditions by acquiescence, but there would be an agreement if the wholesalers acquiesced to assist in policing the RPM scheme, a criticism that will be reiterated by Justice Harlan in *Parke, Davis*.[36]

28. U.S. v. Bausch & Lomb Optical, 321 U.S. 707 (1944)

29. *Id.* at 723.

30. *Id.*

31. *Id.*

32. *Id.* at 714-15. However, the district court did find that there were agreements between the defendant and its wholesalers.

33. *Id.* at 723.

34. *Id.*

35. *See* Robinson, *supra* note 24, at 584 ("In *United States v. Bausch & Lomb Optical Co.*, the Court went one step further, holding that employing wholesalers in a scheme of enforcement constituted a 'combination' with them, even if the wholesalers merely acquiesced in the manufacturer's scheme."); Floyd, *supra* note 18, at 289-90 ("After a twenty-year hiatus, the Court in *United States v. Bausch & Lomb Optical Co.* reconfirmed the implications of *Beech-Nut* by declining to draw a sharp line between voluntary 'agreements' on the one hand and coerced compliance or acquiescence on the other.").

36. Floyd, *supra* note 18, at 290 ("After Bausch & Lomb, . . . [there would be a violation] so long as the alleged conspirators had done more than acquiesce in setting their own resale prices, but had in some sense 'cooperated'—whether through agreements or coercion and tacit acquiescence being immaterial—in the implementation of a supplier's plan of resale price

There is also language in the majority opinion suggesting that the Supreme Court may have taken a more holistic approach to the issue of agreement. The Court observed that:

> The requirement of the wholesalers' recommendation as to the business character of the applicant for a retail license, the evidence of espionage, the limitation of resales to Soft-Lite[37] retail licensees, the existence of the 'Protection Certificate' to mark the wholesaler who might violate the arrangement, the uniformity of the prices, as prescribed in Soft-Lite's published lists, which retailers are charged by wholesalers – all amply support, indeed require, the inference of the trial court that a conspiracy to maintain prices down the distribution system existed between the wholesalers and Soft-Lite through the years prior to this suit.[38]

It is instructive to examine each of the facts upon which the Court relied to substantiate a finding of an agreement. The requirement of a wholesaler's recommendation to grant a retail license can be interpreted as the wholesaler's concurrence that a particular retailer will abide by the minimum prices and is therefore suitable for inclusion in the RPM scheme. It, however, does not unequivocally indicate a commitment on the part of the wholesalers to sell only to compliant retailers. It at most is only suggestive of such a commitment. Evidence of espionage is similar to the use of salesmen and agents to monitor compliance in *Beech-Nut*. The Court did not explicitly state who conducted the espionage. Earlier in the opinion, the Court referred to "surveillance through Soft-Lite's salesmen."[39] If this is what the Court was referring to, the monitoring work did not involve third-party intermediaries and was only done by the defendant's own employees. Reliance on this factor would be equally subject to the criticism of the dissent in *Beech-Nut*. The limitation of resale to Soft-Lite retail licensees could be the result of nothing more than a unilateral refusal to sell to non-compliant retailers, and hence should not support a finding of an agreement. The "Protection Certificate" arrangement is similar to Beech-Nut's use of numbers and symbols to facilitate the tracing of its products[40] and again should be unobjectionable. Lastly, the Court cannot rely on price uniformity as a supporting fact for an agreement, as price uniformity would also result if the RPM scheme was enforced only by unilateral conduct. In short, the only relevant fact is that wholesaler's recommendation is required for a retail

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maintenance through restricted dealing, reporting of price-cutters, or similar 'cooperative methods.'").

37. Soft-Lite was the Bausch & Lomb subsidiary that was at issue in the case.
38. U.S. v. Bausch & Lomb Optical, 321 U.S. 707 (1944).
39. *Id.* at 716.
40. *Id.* at 714.

license, which can be construed as circumstantial evidence that there is an agreement between the wholesalers and the defendant.

6. United States v. Parke, Davis & Co.

The next RPM case to reach the Supreme Court was *United States v. Parke, Davis & Co*.[41] The Supreme Court again found that there was an illegal agreement to enforce an RPM scheme on two principal grounds.[42] First, Parke, Davis "used the refusal to deal with the wholesalers in order to elicit their willingness to deny Parke Davis products to retailers and thereby help gain the retailers' adherence to its suggested minimum retail prices."[43] In doing so, Parke, Davis "created a combination with the retailers and the wholesalers to maintain retail prices and violated the Sherman Act."[44] Second, Parke, Davis entered into negotiations with individual retailers to secure their agreement to suspend advertising of discounted products.[45] Distilling from the holding of *Beech-Nut* and *Bausch & Lomb*, the Court asserted the following:

> [A]n unlawful combination is not just such as arises from a price maintenance *agreement*, express or implied; such a combination is also organized if the producer secures adherence to his suggested prices by means which go beyond his mere declination to sell to a customer who will not observe his announced policy.[46]

This seems to suggest that any effort to enforce an RPM scheme beyond a mere announcement of a refusal to sell would render an RPM scheme an illegal agreement. The Court hinted that the reason it objected to enforcement effort beyond mere announcement was its coercive effects on retailers.[47] The only permissible kind of acquiescence is one that results from "a matter of individual free choice prompted alone by the desirability of the product."[48] An important acknowledgment made by the Court in the case was that the economic effects of an illegal RPM agreement are the same as one resulting from a unilateral refusal-to-deal policy permissible under *Colgate*.[49] This calls into question the soundness of the *Colgate* doctrine

41. United States v. Parke, Davis & Co., 362 U.S. 29 (1960).
42. *Id.* at 45.
43. *Id.*
44. *Id.*
45. *Id.* at 46.
46. *Id.* at 43.
47. *Id.* at 46-47.
48. *Id.* at 47.
49. *Id.* at 44 ("True, there results the same economic effect as is accomplished by a prohibited combination to suppress price competition if each customer, although induced to do so solely by a manufacturer's announced policy, independently decides to observe

from an economic perspective, an argument that will be pursued subsequently.

Parke, Davis stands for the proposition that a supplier cannot enlist the assistance of intermediaries such as wholesalers to enforce an RPM scheme, even if the assistance is enlisted not through an outright agreement, but from mere acquiescence of the wholesalers.[50] Condemnation of the use of intermediaries has been a running theme since *Beech-Nut*.[51] *Parke, Davis* merely reaffirmed it in starker terms, as the wholesalers' involvement was rather minimal compared to that in *Beech-Nut* and *Bausch & Lomb*.

This theory of an RPM agreement has been subject to considerable criticisms. Justice Harlan in his dissent questioned why voluntary acquiescence to a supplier's unilateral policy on the retailer level is not illegal but becomes so when the same acquiescence is made simultaneously at the wholesaler level.[52] A number of commentators have noted the same flaw in this theory.[53] This is especially so because by interposing wholesalers between the supplier and the retailers, there is no direct contact between the supplier and the retailers, and the relationship between them becomes more remote.[54] The holding in *Parke, Davis* favors markets in which the supplier can effectuate an RPM scheme without the help of intermediaries, most likely where the supplier does not use wholesalers. It effectively gives suppliers that sell directly to retailers greater liberty to effectuate an RPM scheme, a result that is arbitrary and devoid of economic justifications.

Criticisms notwithstanding, *Parke, Davis* can be understood to have lent further support to the enforcement and the coercion theories of

specified resale prices. So long as Colgate is not overruled, this result is tolerated but only when it is the consequence of a mere refusal to sell in the exercise of the manufacturer's right 'freely to exercise his own independent discretion as to parties with whom he will deal.'").

50. *See* Hovenkamp, *supra* note 24, at 9 (stating that the *Parke, Davis* court relied on Parke, Davis' use of wholesalers to enforce its RPM scheme rather than the voluntary acquiescence of retailers in finding a manufacturer combination); Levi, *supra* note 9, at 262 ("There is no evidence that any of them [wholesalers] made any agreement with Parke, Davis as to prices or that Parke, Davis ever solicited an agreement from any of them as to this matter.").

51. Levi, *supra* note 9, at 325.

52. United States v. Parke, Davis & Co., 362 U.S. 29, 55 (1960).

53. *See* Edward O. Correia, *Resale Price Maintenance—Searching for a Policy*, 18 J. LEGIS. 187, 192 (1992) ("By involving the wholesaler, the supplier has still not obtained any assurance from the retailer as to future pricing practices. It has simply used the same technique of influencing behavior through threatening termination at the wholesaler level."); Floyd, *supra* note 18, at 294 ("[T]here is an inherent conflict between recognizing a combination among manufacturers, wholesalers, and retailers (because both wholesalers and retailers could be terminated for refusing to comply) yet refusing to recognize a combination when retailers alone comply in order to avoid termination.").

54. Correia, *supra* note 53, at 192.

agreement.[55] The former holds that an illegal RPM agreement is found when the supplier undertakes enforcement effort beyond a certain level. *Parke, Davis* itself seemed to have set that level as anything beyond mere announcement of a policy of unilateral refusal to deal, which is a very strict standard. The latter asserts that an illegal RPM agreement is found if a retailer is subject to pressure beyond the inherent attractiveness of the product to comply with the supplier's demand.

7. Albrecht v. Herald Co.

The next Supreme Court case that is relevant to the agreement issue is *Albrecht v. Herald Co.*[56] The case involved vertical maximum price fixing. The case did not raise the issue of when an agreement exists between the supplier and the retailer; it instead focused on what kind of agreement sufficed for the purpose of establishing a violation of Section 1. The dealer in that case refused to abide by the vertical maximum prices set up by a newspaper publisher and the publisher attempted to coerce the dealer to comply by soliciting assistance of a third-party delivery company and a third-party solicitation agent.[57] There was clearly no agreement between the newspaper publisher and the non-compliant dealer on vertical maximum prices. Thus, there arose the issue of whether there was an illegal agreement in the case. The Court held that the requisite agreement was found between the newspaper publisher on the one hand and the solicitation agent and the delivery company on the other hand.[58] Even though the two third parties had no financial interest in the success of the vertical maximum price fixing scheme, the Court thought that the agreements between them and the publisher sufficed because the third parties were aware of their role in the price fixing scheme and knew that their service would no longer be required if the non-compliant dealer succumbed.[59]

Footnote 6 of the opinion indicated an even more expansive understanding of the notion of an agreement.[60] Burns argued that the Court's view on agreement in this case is so broad that "it came close to holding that there was no legal two-party vertical arrangement, at least if it involved prices."[61] The Court suggested that in addition to the agreement between the

55. Hovenkamp, *supra* note 24, at 9.
56. Albrecht v. Herald Co., 390 U.S. 145 (1968).
57. *Id.* at 147.
58. *Id.* at 149-50.
59. *Id.* at 150.
60. *Id.* at 150 n.6. It has been noted that the understanding of agreement expressed in this footnote gained substantial acceptance by the courts, at least until *Monsanto*. Floyd, *supra* note 18, at 292.
61. Jean Wagman Burns, *Rethinking the "Agreement" Element in Vertical Antitrust*

publisher and the third parties, the plaintiff could have relied on three other agreements as well.[62] The first one is that between the publisher and the plaintiff, at least as of the date the plaintiff finally succumbed to the defendant's pressure.[63] The second one is that between the publisher and other compliant dealers.[64] The third one, perhaps rather surprisingly, is that between the publisher and the final consumers, the newspaper readers; the publisher, for a period, sold newspapers directly to the end consumers with the help of the third parties.[65] Justice Harlan heavily criticized the majority's treatment of the agreement issue. In particular, he argued that the majority's reliance on the agreement between the defendant and the two third-party agents and the suggestion that the agreement between the defendant and other compliant dealers would have sufficed is misguided.[66]

Justice Harlan argued that the third parties had no economic interest in the relationship between the publisher and the non-compliant dealer.[67] It is, strictly speaking, not true that the third parties had no economic interest in the behavior of the non-compliant dealer. They would be terminated as soon as the non-compliant dealer capitulated. They therefore preferred continual non-compliance. What is true is that their economic interest is different from, and contrary to, the interest of the publisher in maintaining the vertical maximum price fixing scheme. With respect to the agreement with the compliant dealers, Justice Harlan argued that as opposed to the typical RPM situation where each dealer had an interest in the maintenance of the policy as deviation by one would harm all, the dealers had no interest in how each other's territory was administered in *Albrecht*.[68] The dealers' territories operated separately. Justice Harlan can be understood to have propounded another theory of agreement under vertical restraints: the economic interest theory, which holds that an agreement should not be considered for the purpose of a Section 1 violation if either party to the agreement does not have an economic interest in the success of the allegedly illegal scheme.[69]

Restraints, 51 OHIO ST. L.J. 1, 19 (1990).

62. Albrecht v. Herald Co., 390 U.S. 145, 150 n.6 (1968).

63. *Id.*

64. *Id.*

65. *Id.*

66. *Id.* at 158-60.

67. *Id.* at 161 ("Once it is recognized that Kroner had no interest whatever in forcing his competitor to lower his price, and was merely being paid to perform a delivery job that respondent could have done itself, it is clear respondent's activity was in its essence unilateral.").

68. *Id.* at 161.

69. This theory probably is less relevant to the RPM context as most of the parties involved have a stake in the maintenance of the RPM. When one dealer defects, every other dealer operating in the same market will be affected. One scenario in which this may not be the case is if retailers operate in different geographical areas or customer segments and the

Lastly, reference should be made to a prescient comment made by Justice Harlan concerning the role of agreement in the law on vertical restraints. He argued that:

> The Court's difficulties on all of its theories stem from its unwillingness to face the ultimate conclusion at which it has actually arrived: it is unlawful for one person to dictate price floors or price ceilings to another; any pressure brought to bear in support of such dictation renders the dictator liable to any dictatee who is damaged. The reason for the Court's reluctance to state this conclusion bluntly is transparent: this statement of the matter takes no account of the absence of a combination or conspiracy.[70]

Although this comment was made in the context of vertical maximum price fixing, it resonates in the string of RPM cases that have been examined so far. Given how far the *Colgate* doctrine has been pared back and the endorsement of the coercion theory in *Parke, Davis* and *Albrecht*[71], one may question whether the Court has effectively condemned unilaterally imposed RPM.

8. Perma Life Mufflers v. International Parts Corp.

In the same year as *Albrecht*, the Supreme Court decided *Perma Life Mufflers v. International Parts Corp.*, which, although strictly speaking was not concerned with the agreement issue, sheds light on the Court's understanding of the relationship between coercion and agreement.[72] The issue in the case was whether distributors who had adopted a variety of vertical restraints, including exclusive dealing, tying, exclusive territory, and RPM, under pressure from the manufacturer were barred from recovery under the antitrust law by the *in pari delicto* doctrine.[73] The Court held that the distributors were not barred from recovery by the *in pari delicto* doctrine even though they had adopted the vertical restraints imposed by the

plaintiff is trying to establish an agreement between the supplier and one retailer by referring to an agreement between the supplier and retailers operating in another territory or another customer segment.

70. *Id.* at 162

71. *See* Correia, *supra* note 53, at 192 ("Thus, the Court reasoned, if *Parke Davis* recognized an agreement based on coercion of retailers through the use of wholesalers, an agreement would also be formed if a supplier coerced a dealer to charge a particular price through the use of an agent soliciting away the dealer's customers. Moreover, the Court stated that an agreement for purposes of the Sherman Act could be found based on unwilling compliance by the coerced dealer.").

72. Perma Life Mufflers, Inc. v. Int'l Parts Corp., 392 U.S. 134 (1968) (holding that the doctrine of *in pari delicto* is not a defense in an antitrust action), *overruled by* Copperweld Corp. v. Indep. Tube Corp., 467 U.S. 752 (1984).

73. *Id.* at 137-38.

defendant.[74] The Court noted that the distributors' "participation was not voluntary in any meaningful sense."[75] It acknowledged that the distributors sought the franchises enthusiastically, but only acceded to the vertical restraints "because their acquiescence was necessary to obtain an otherwise attractive business opportunity."[76] In his concurrence, Justice White noted that subject to the market power and leverage of a powerful counterparty, the plaintiff "was unwilling to enter the illegal scheme, was motivated principally by what he thought was economic necessity — the need to avoid losing business by being unable to offer a major product line[.]"[77] Therefore, the distributors should not bear equal responsibility for the conduct and should not be barred from recovery.

This case is particularly noteworthy for the observation that coercion does not elicit assent that is voluntary in any meaningful sense. If an agreement is understood to be a voluntary meeting of the minds, then an agreement brought about through coercion does not qualify. Moreover, the opinion suggests that the Court's threshold for coercion or undue pressure is quite low.[78] The opinion did not mention any specific acts of coercion that were found in some of the earlier cases, such as *Parke, Davis*. It seems that the defendant did not undertake any affirmative acts to solicit compliance apart from "the communicated danger of termination[.]"[79] Lastly, the Court implicitly endorsed the economic interest theory. The Court argued that the distributors should not bear responsibility for the exclusive dealing requirement and the full-line product requirement because these two restraints were clearly against their economic interest.[80] The implicit argument is that the distributors should not be deemed to have voluntarily assented to these restraints when the restraints were against their economic interest.

9. Monsanto Co. v. Spray-Rite Service Corp.

In the 1980s, the Supreme Court decided two important cases on the notion of agreement in vertical restraint cases, *Monsanto Co. v. Spray-Rite*

74. *Id.* at 140.
75. *Id.* at 139.
76. *Id.*
77. *Id.* at 145-46.
78. *Id*. at 155 (Harlan, J., concurring) (suggesting that the plaintiffs could potentially benefit from the "coercion" exception to the *in pari delicto* doctrine, although the majority did not use the term "coercion" to refer to the defendant's conduct).
79. *Id.* at 142 (quoting United States v. Arnold, Schwinn & Co., 388 U.S. 365, 372 (1967)).
80. *Id.* at 140-41.

Service Corp.[81] and *Business Electronics Corp. v. Sharp Electronics Corp*.[82] Both cases differ from the previous cases in a number of significant ways. First, both cases involved dealer termination, in which the Court was asked to infer a vertical price fixing agreement from the act of termination.[83] Although inference of an RPM agreement from circumstantial evidence is nothing new, what is different is that dealer termination itself could be anticompetitive under certain circumstances. That is not true of the conduct from which the Court was asked to infer an agreement in the previous cases. In these two cases, the plaintiffs did not pursue dealer termination as an antitrust violation directly, probably because at the time, resale price maintenance was still illegal *per se*. However, that is no longer the case after *Leegin* and it is worth exploring decoupling RPM from dealer termination and treating each as an independent violation. Second, although the Court did rule for the plaintiff in *Monsanto*, these two cases reversed the hitherto long-term trend of pro-plaintiff outcomes in Supreme Court RPM cases. The Supreme Court significantly tightened the requirement for a showing of an agreement in RPM cases.[84] It is worth exploring the continual relevance of the cases from the previous decades after *Monsanto* and *Business Electronics*.

In *Monsanto*, at issue was whether an RPM agreement could be inferred from the existence of dealer complaints and termination that followed or even came about in response to the complaints.[85] Monsanto had terminated a price-cutting distributor Spray-Rite following complaints from other distributors.[86] Spray-Rite brought suit, alleging that its termination was part

81. Monsanto Co. v. Spray-Rite Serv. Corp., 465 U.S. 752 (1984) (holding that to find existence of a vertical price-fixing agreement, something more than evidence of complaints by other distributors is needed and the jury should determine whether the plaintiff was terminated because of price-fixing conspiracy between the manufacturer and distributors).

82. Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717 (1988) (holding that vertical restraint of trade is not per se illegal under the Sherman Act unless it includes agreement about price).

83. These two cases are dealer termination cases perhaps because they were both brought by private litigants as opposed to the government, unlike in a vast majority of the RPM cases in the previous decades. Private RPM cases would almost by definition involve dealer termination. If the dealer complies with the minimum prices, there would be no case to bring. Only when a dealer refuses to comply with these prices and is terminated would he have an incentive to sue. It is of course possible for a dealer to sue when a manufacturer refuses to trade with the dealer for his refusal to abide by the RPM scheme. But such a suit would be more challenging as it would be more difficult for the plaintiff to prove that it has suffered injury.

84. This may be partly due to the fact that both cases were private action and the Court was careful not to encourage excessive dealer termination cases.

85. *Monsanto,* 465 U.S. at 759.

86. *Id.*

of an illegal RPM scheme Monsanto had put in place.[87] The Supreme Court held that the existence of dealer complaints and termination that came about in response to those complaints is not alone sufficient to substantiate an illegal vertical price fixing agreement.[88] Instead, "[t]here must be evidence that tends to exclude the possibility that the manufacturer and non[-]terminated distributors were acting independently."[89] Under this standard, "the antitrust plaintiff should present direct or circumstantial evidence that reasonably tends to prove that the manufacturer and others 'had a conscious commitment to a common scheme designed to achieve an unlawful objective.'"[90] The Court gave a number of reasons for its holding. First, the Court reiterated that under *Colgate*, there is an important distinction between permissible unilateral action and illegal concerted action.[91] Second, the Court argued that a heightened evidentiary standard is necessary to preserve the dividing line between the rule of reason for vertical non-price restraints and the *per se* rule for vertical price restraints.[92] Third, the Court cautioned against attaching too much weight to dealer complaints because a manufacturer who has legitimate business needs to have constant communication with its dealers and dealers are an important source of

87. *Id.* at 757.

88. *Id.* at 763; *but see* Floyd, *supra* note 18, at 274 (stating that most of the appellate courts that had considered the issue had held that such evidence was sufficient to create a jury issue on whether the manufacturer and the complaining dealers acted in concert); *id*. at 275 (arguing that upon showing of such evidence, the burden should shift to the defendant to show that it was acting unilaterally).

89. *Monsanto*, 465 U.S. at 764, *questioned in* Floyd, *supra* note 18, at 274 (criticizing the Court's holding as inconsistent with general rules on the sufficiency of evidence to create a jury issue by stating that a plaintiff "need not introduce evidence excluding all possible circumstances that would defeat liability, so long as the evidence that it does produce is sufficient to permit a reasonable inference that would support liability").

90. *Monsanto*, 465 U.S. at 764 (quoting Edward J. Sweeney & Sons, Inc. v. Texaco Inc., 637 F.2d 105 (3rd Cir. 1980), *cert denied*, 451 U.S. 911 (1981)).

91. *Monsanto*, 465 U.S. at 761; *See* Burns, *supra* note 61, at 23-24 ("Yet, to separate such legal communications and distribution arrangements from illegal ones, the Court once again fell back on the 'unilateral action' versus 'agreement' distinction of Colgate. Under this approach, the Court concluded that complaints from distributors about other price-cutting distributors are 'natural' and not indicative of 'illegal concerted action,' and that merely showing that a manufacturer acted in response to such complaints did not, by itself, prove the existence of an unlawful agreement. The manufacturer could have received the complaints and communicated with its dealers but nonetheless have acted unilaterally.")

92. *Monsanto*, 465 U.S. at 762; *but see* Jeffrey L. Harrison, *Dr. Miles's Orphans: Vertical Conspiracy and Consignment in the Wake of Leegin*, 45 WAKE FOREST L. REV. 1125, 1142 (2010) (arguing that the Court did not address the issue of the distinction between price and non-price restraints head-on, but instead tinkered with the evidentiary standard for an agreement and that the Court could have required lower courts to give clear instructions to the jury on the distinction between vertical price and non-price restraints).

information for the manufacturer.[93] Allowing a plaintiff to establish an agreement based on dealer complaints and termination in response to them would threaten to strangle such communication.

Applying this new evidentiary standard, the Court held that there was sufficient evidence in the case to establish an RPM agreement between the defendant and its dealers.[94] First, there was evidence that the defendant actively solicited compliance from a price-cutting dealer through communication with its parent company, upon which the dealer gave assurance to Monsanto that it would abide by the minimum resale prices.[95] Second, the Court referred to a newsletter from one of Monsanto's distributors that made some reference to an arrangement.[96] The Court argued that this reference could be interpreted as reference to a price fixing agreement.[97]

It is difficult to determine the extent to which *Monsanto* modified the prior case law on the existence of agreement. This is because the factual scenario and focus of inquiry in *Monsanto* are quite different from those in the previous cases. In *Monsanto*, the question was not how much more a supplier can do beyond mere unilateral announcements without creating an illegal agreement. Assuming that the RPM scheme in *Monsanto* was implemented through unilateral announcements, the one additional step Monsanto took was the termination of Spray-Rite, which was clearly permitted under *Colgate*. As it turns out, Monsanto went beyond making unilateral announcements — it sought assurances from non-compliant dealers — which means that there was clearly an illegal agreement under the *Colgate* line of cases. Instead, the question in *Monsanto* was about to what extent parallel action by independent actors can be interpreted as constituting an agreement, the parallel action here being dealer complaints and termination by the supplier, both of which could have happened with or without an agreement between the supplier and the complaining dealer. The Court held that if the parallel action can be given an innocuous and an anticompetitive explanation equally plausibly, the former is to be preferred.[98] Thus, *Monsanto* dealt with different questions from the ones posed in the previous cases and the *Colgate* line of cases was arguably left undisturbed.

Floyd asserted the contrary view: that the *Colgate* line of cases did not

93. *Monsanto*, 465 U.S. at 763.
94. *Id.* at 765.
95. *Id.*
96. *Id.* at 765-766.
97. *Id.* at 766, *questioned in* Calvani & Berg, *supra* note 9, at 1198 (arguing that the Court's reliance on the ambiguous evidence of a newsletter as sufficient evidence provides little guidance to counsel on the sufficiency of evidence).
98. Robinson, *supra* note 24, at 599.

survive *Monsanto*.[99] He argued that:

> If, as the Supreme Court has now announced in Monsanto, the *sine qua non* of illegality is not only a 'conscious commitment to a common scheme designed to achieve an unlawful objective', but also a showing that 'the distributor communicated its acquiescence or agreement, and that this was sought by the manufacturer', it is difficult to see how *Parke*, *Davis*, *Beech-Nut* and related decisions can survive.[100]

This was with reference to footnote 9 of the opinion. Floyd overstated the impact of *Monsanto* on the *Colgate* line of cases. Footnote 9 states that:

> The concept of "a meeting of the minds" or "a common scheme" *in a distributor-termination case* [emphasis added] includes more than a showing that the distributor conformed to the suggested price. It means as well that evidence must be presented both that the distributor communicated its acquiescence or agreement, and that this was sought by the manufacturer.[101]

This footnote imposes a new communication requirement on agreements in the context of vertical price restraints and would have implicitly overturned the longstanding rule in the *Colgate* line of cases that an agreement can be implied from circumstantial evidence had the Court not limited this new rule to dealer termination cases. This rule has a much more limited scope. It does not say that every vertical price fixing agreement must be substantiated with evidence of communication between the supplier and the dealer concerning assurance of compliance. Instead, it effectively says that a vertical price fixing agreement cannot be inferred solely from dealer termination. It must be substantiated with additional evidence. In fact, it is unclear the Court even applied the rule faithfully in the case. In addition to the evidence that Monsanto sought assurance of compliance from a distributor through its parent company, the Court also relied on the ambiguous evidence of the newsletter. If evidence as ambiguous as the newsletter would suffice, the Court in effect required much less than express communication between the supplier and the dealers.[102]

One may in fact argue that the Court's detailed analysis of the issue of the sufficiency of dealer termination in response to dealer complaints as

99. *See also* Correia, *supra* note 53, at 198 (noting that after *Monsanto* and *Business Electronics* it has become very difficult to establish liability in dealer termination cases).

100. Floyd, *supra* note 18, at 298 (quoting Monsanto Co v. Spray-Rite Service Corp., 465 U.S. 752, 764 n.9 (1984)).

101. *Monsanto*, 465 U.S. at 764 n.9.

102. However, admittedly, one can argue that the Court used the newsletter as additional evidence to bolster the primary evidence of Monsanto seeking assurance from a distributor through its parent company.

proof of an agreement is much ado about nothing. The fact that Monsanto sought assurances of compliance with its RPM scheme through the parent company of a distributor and obtained the assurance from the distributor subsequently was more than sufficient to support the finding of an RPM agreement under the standard laid down by the previous cases.[103] A simple application of the *Colgate* doctrine would have led to the conclusion that there was an agreement. *Colgate* only allows unilateral announcement of policy and forbids seeking of assurances from dealers. Moreover, the parent company can be characterized as an intermediary, and the use of an intermediary to ensure compliance was held to be sufficient to support a finding of agreement under *Parke, Davis*.[104] Therefore, without resorting to any new evidentiary standard, the Court could have arrived at the same conclusion. *Monsanto* added nothing new to the issue of the existence of agreement in vertical price restraints. The only issue that needed to be addressed in the case was whether the termination was pursuant to the price fixing scheme, which the Court dealt with in fairly summary fashion.

One is not even sure about the significance of the distributor termination in determining Monsanto's liability. The Court did not seem to suggest that dealer termination is an independent antitrust violation, at least in the factual context of the case. The focus of the inquiry was whether there was an illegal RPM scheme. Once there was direct evidence of an agreement between Monsanto and its compliant distributors, the question of inferring the existence of an illegal vertical price fixing agreement from dealer termination in response to complaints became superfluous. Consequently, one may argue that the real issue in *Monsanto* was not the existence of an agreement in vertical price restraints, but the legality of dealer termination. Under *Colgate*, it is legal for a supplier to terminate a dealer that refuses to comply with the minimum prices set by the supplier. The twist presented in *Monsanto* was whether it would make any difference if the termination was made in response to dealer complaints. Dealer complaints may indicate anticompetitive potential because it is possible that the supplier would have tolerated price cutting by the non-compliant dealer and would not have terminated that dealer but for the complaints.[105] In that case, the termination

103. This has led Correia to comment on the fortuitous nature of the case. The only reason the plaintiff was able to prove an agreement was the non-compliance of one of the dealers. If there had been complete compliance in the scheme, Spray-Rite would have been out of luck. Correia, *supra* note 53, at 203.

104. *See* U.S. v. Parke, Davis & Co., 362 U.S. 29, 45 (1960) (finding that Parke Davis had committed illegal vertical price fixing when it used its wholesalers to deny products to uncooperative retailers).

105. *See* Correia, *supra* note 53 at 197 ("[T]erminating a discounting dealer certainly affects the degree of price competition among dealers. By agreeing to eliminate the discounter, the supplier and the remaining dealer have reduced price competition at the retail

was made under pressure from the complaining dealer to shield that dealer from price competition.[106] The Court's answer was that dealer termination in response to complaints would only be illegal if it was made in the context of an illegal vertical price fixing scheme, which was further substantiated by evidence of communication of assurance between the supplier and the complaining dealers.[107]

What is the significance of the vertical price fixing scheme to the anticompetitive potential of complaint-motivated dealer termination? Does the existence of a vertical price fixing scheme render the termination more anticompetitive? The answer would seem to be no. If a powerful dealer uses its bargaining power to pressure the supplier to terminate a price-cutting dealer, the result is the same regardless of whether there is a vertical price fixing scheme: the elimination of a source of price competition on the dealer level. To the extent that intrabrand competition is important to protect, this elimination raises a competitive concern. In fact, the Court's requirement that the termination be made in the context of a vertical price fixing scheme is almost counter-intuitive. The existence of such a scheme means that there is a greater likelihood that the supplier would have independently wanted to terminate the price-cutting dealer, which would render the termination less anticompetitive and more permissible, since the supplier would only be exercising its right under *Colgate*. Complaint-motivated dealer termination would be more problematic if the supplier does not have a strong preference over resale price and yet terminates a price-cutting dealer under pressure from another dealer.

This leads to another anomaly in the *Monsanto* case. In discussing whether Monsanto's termination of Spray-Rite was pursuant to its RPM scheme, the Court suggested that Monsanto's attribution of the termination to Spray-Rite's performance was pretextual and that Monsanto was ultimately motivated by Spray-Rite's price cutting.[108] The Court noted that the first thing a Monsanto official mentioned in a post-termination meeting with Spray-Rite was the latter's prices.[109] The Court further noted that

level.").

106. *Monsanto*, 465 U.S. at 765.

107. *Id.* at 768. The Court's application of this rule to the facts of the case suggests that the Court may not have been entirely convinced about the rule itself. This possible lack of conviction notwithstanding, one questions why the Court decided to impose a higher evidentiary standard on the proof of an agreement in a dealer termination case than the usual RPM cases, which do not require proof of communication. One possible reason is perhaps that dealer termination cases are almost by definition private cases, and the Court was getting increasingly concerned about the flood of dealer termination cases in the federal courts. The Court hence wanted to deter these cases by imposing a higher evidentiary standard.

108. *Monsanto*, 465 U.S. at 765.

109. *Id.* at 767.

Monsanto never discussed with Spray-Rite the criteria which allegedly formed the basis for Spray-Rite's termination.[110] But it was unclear why it would have been more problematic if Monsanto had terminated Spray-Rite due to its price cutting. *Colgate* clearly stated that a supplier has the full right to terminate a dealer who refuses to abide by its minimum resale prices. It would not have mattered what Monsanto's real reason was for terminating Spray-Rite. Under *Colgate*, Monsanto would have the right to terminate Spray-Rite for any reason, including price cutting. Instead, the Court should have focused on whether Monsanto would have terminated Spray-Rite absent dealer complaints. The termination would have been much more problematic if Monsanto would not have done so.

Monsanto also highlights one of the incongruities of the *Colgate* doctrine in light of the coercion theory of agreement. Under the *Colgate* progeny, if a supplier undertakes extra measures, such as making use of wholesalers and marking the products for easy tracing, to coerce a dealer to comply with the RPM scheme, an illegal agreement would arise. But under *Colgate*, it would be perfectly legal for the supplier to use its ultimate weapon of coercion: termination. This creates a situation where a supplier must refrain from using a moderate amount of coercion, but instead can legally use the most coercive weapon. One can argue that the difference is that in the case of moderate coercion, the dealer complies and abides by the RPM scheme. In the case of termination, the dealer ultimately refuses to comply. However, if that is the basis for deciding whether there is an illegal agreement, it seems to be no longer about the presence of coercion, but about whether there is a meeting of the minds and compliance with the scheme.

10. Business Electronics Corp. v. Sharp Electronics Corp.

Business Electronics Corp. is another dealer termination case decided by the Supreme Court in the 1980s.[111] In that case, the defendant Sharp Electronics had terminated the plaintiff Business Electronics as a retailer for its calculators after receiving complaints from another retailer, Hartwell.[112] At issue was whether the dealer termination was governed by the *per se* rule or the rule of reason.[113] The Court formulated the issue as one concerning the dividing line between vertical price restraints which were at the time *per se* illegal and vertical non-price restraints which were subject to the rule of reason.[114] The Court held that the *per se* rule does not apply to dealer

110. *Id.*
111. Bus. Elec. Corp. v. Sharp Elec. Corp., 485 U.S. 717 (1988).
112. *Id.* at 721.
113. *Id.* at 720.
114. *Id.* at 725.

termination absent a further agreement on the price or price levels to be charged by the remaining dealers.[115] The Court justified this holding on the grounds that in dealing with vertical restraints, there is a presumption in favor of the rule of reason.[116] This is because a liberal application of the *per se* rule would erode the protection afforded by *GTE Sylvania*[117] of vertical non-price restraints and the solicitude the Court had expressed in the case for interbrand competition.[118]

Similar to *Monsanto*, the focus in *Business Electronics* is on when dealer termination would be illegal, and not how much more a supplier can do beyond mere announcements to enforce an RPM scheme. The Court in *Business Electronics* went one step further than the *Monsanto* court. In *Monsanto*, the Court had held that ambiguous common action by the supplier and complaining dealers is not sufficient to establish a violation of the antitrust law.[119] In *Business Electronics*, the Court held that even an agreement between a supplier and a complaining dealer is not enough to establish a violation.[120] There must be showing of a concomitant vertical price fixing agreement.[121] This is because a dealer may have been terminated for violation of a vertical non-price restraint as opposed to a vertical price restraint. In order to guard against false positives, dealer termination would only be subject to the *per se* rule when there was clear evidence of a vertical price fixing agreement.[122] The Court, however, said nothing in the opinion about how this vertical price fixing agreement could be proved. Therefore, one can presume that the approaches laid down in the pre-*Monsanto* cases

115. *Id.* at 727.

116. *Id.* at 726.

117. Continental T.V., Inc., et al. v. GTE Sylvania Inc., 433 U.S. 36 (1977).

118. *See Bus. Elec.*, 485 U.S. at 726 (stating that "interbrand competition is the primary concern of the antitrust laws; and that rules in this area should be formulated with a view towards protecting the doctrine of *GTE Sylvania*").

119. *Monsanto*, 465 U.S. at 763-64 ("On a claim of concerted price fixing, the antitrust plaintiff must present evidence sufficient to carry its burden of proving that there was such an agreement. If an inference of such an agreement may be drawn from highly ambiguous evidence, there is considerable danger that the doctrines enunciated in *Sylvania* and *Colgate* will be seriously eroded. . . . There must be evidence that tends to exclude the possibility that the manufacturer and non[-]terminated distributors were acting independently.").

120. *Bus. Elec.*, 485 U.S. at 726-27 ("There has been no showing here that an agreement between a manufacturer and a dealer to terminate a 'price cutter,' *without a further agreement on the price or price levels to be charged by the remaining dealer*, almost always tends to restrict competition and reduce output. Any assistance to cartelizing that such an agreement might provide cannot be distinguished from the sort of minimal assistance that might be provided by vertical non[-]price agreements like the exclusive territory agreement in *GTE Sylvania*, and is insufficient to justify a *per se* rule." (emphasis added)).

121. *Id.* at 735-36.

122. Harrison, *supra* note 92, at 1142.

continue to apply.[123]

Given that the main justification for the rule in *Business Electronics* is the preservation of the divide between the different legal rules that applied to vertical price and non-price restraints, the case lost much of its significance after the divide was removed by *Leegin*. The residual

123. Correia, however, argued that *Business Electronics* has rendered the holding of *Monsanto* largely moot:

> *Sharp*, in most cases, makes the evidentiary hurdles erected by *Monsanto* moot. Even if the plaintiff can prove that the supplier who terminated it agreed with a complaining dealer about the termination, it is unlikely to prove that the complaining dealer and the supplier agreed on the complaining dealer's prices.

Correia, *supra* note 53, at 211. More damagingly, Harrison argued that *Business Electronics* had practically ended the *per se* rule under *Dr. Miles* because after *Business Electronics*, courts have come to require an agreement on the actual price level to warrant the *per se* rule:

> *Business Electronics*, for all practical purposes, ended the reign of *Dr. Miles*. After *Business Electronics*, evidently the only way to engage in unlawful RPM was to not only have just an agreement stabilizing resale price, but also have an agreement on the actual price level . . . . After *Business Electronics*, it was clear that agreements except those pegging a specific price were also exempt. Indeed, after *Monsanto* and *Business Electronics*, findings that firms have engaged in per se unlawful RPM are rare.

Harrison, *supra* note 92, at 1143; *see also* Burns, *supra* note 61, at 27-28 (explaining how the *Business Electronics* holding made findings of purely vertical per se illegal restraints obsolete). Harrison's prognosis of the impact of *Business Electronics* reflects a careless reading of the case. To the extent that his description of the lower courts' treatment of *Business Electronics* was true, the lower courts have misread *Business Electronics*.

A careful reading of the case shows that Justice Scalia was specifically referring to situations in which there was an agreement to terminate a price-cutting dealer. He noted in the opinion that "[t]here has been no showing here that an agreement between a manufacturer and a dealer to terminate a 'price cutter,' without a further agreement on the price or price levels to be charged by the remaining dealer, almost always tends to restrict competition and reduce output." *Business Electronics*, 485 U.S. at 726-27. Nowhere did the Court assert that this requirement of an explicit agreement on price applies to all RPM schemes, including those without dealer termination. Moreover, in a number of places in the opinion, Justice Scalia referred to the possibility that dealer termination may be the result of enforcement of a vertical price or non-price restraint. One cannot be certain which applies in a particular case simply from observing dealer termination. Although Justice Scalia concluded his opinion with the assertion that "a vertical agreement is not illegal *per se* unless it includes some agreement on price or price levels," *Bus. Elec.*, 485 U.S. at 735-36, viewed holistically, the opinion was clearly addressing situations in which there is dealer termination, and not vertical restraints in general.

In addition, Justice Scalia did not address in his opinion the issue of how an agreement on price can be proved. From the *Colgate* line of cases, it is clear that an agreement on price can be proved from circumstantial evidence, including evidence of coercion or complex enforcement effort. In any case, even if it were true that *Business Electronics* stands for the proposition that there must be some explicit agreement on price or price levels proved by direct evidence, such a strict rule is no longer warranted after the *per se* rule has been overruled in *Leegin*.

significance of the case concerns the legality of dealer termination. The case can be understood to establish the principle that even clearly complaint-motivated dealer termination on its own is not illegal absent a concomitant vertical price fixing agreement. The Court's reasoning can be subject to a number of criticisms. One may argue that the false positive concern Justice Scalia highlighted in the case was concocted out of thin air. As Justice Stevens pointed out in his dissent, nothing in the record suggested that there was a vertical non-price restraint in the case.[124] There was no evidence that Sharp had entered into an exclusive distribution agreement or other kinds of vertical non-price restraints with either Business Electronics or Hartwell.[125]

Moreover, the insistence on evidence of a vertical price fixing agreement is redundant. As argued earlier, such an agreement is only relevant to the extent that it sheds light on the incentives of the supplier to terminate the non-compliant dealer. If Sharp did not have an RPM scheme to protect, it was probably not terribly concerned about resale prices. Sharp could have terminated Business Electronics because of Hartwell's complaints, Business Electronics' own performance, or other legitimate business reasons. Yet in this case, there was no uncertainty as to the impetus for the termination. The jury had found that Business Electronics was terminated because of Hartwell's complaints. Another fact that reinforces the conclusion that Sharp would not have terminated Business Electronics absent Hartwell's complaints is that Hartwell itself had sold below the minimum prices recommended by Sharp.[126] If Sharp had implemented an RPM scheme, it clearly was not a binding one. Sharp was willing to tolerate some deviations by dealers from the recommended prices. Nor should it matter that the supplier and the complaining dealer have a specific agreement on price level, as Justice Scalia required. Complaint-motivated dealer termination is no less anticompetitive simply because the supplier and the complaining dealer did not agree on a specific price level. If a powerful dealer picks out price-cutting dealers one by one by pressuring the supplier to terminate them, intrabrand price competition will still be stifled despite the lack of an agreement on a specific price level.

Justice Scalia argued that dealer termination is only problematic when committed in the context of a vertical price fixing agreement because of the potential of such an agreement to aid cartelization.[127] The implication is that

124. *Bus. Elec.*, 485 U.S. at 739 (Stevens, J., dissenting); Correia, *supra* note 53, at 209 ("Since the supplier was not alleged to have imposed any non-price vertical restraint on its dealers, there was no purpose for terminating the discounting dealer other than eliminating price competition."); Harrison, *supra* note 92, at 1143 (suggesting that vertical agreements that do not specify a specific resale price are legal after *Business Electronics*).

125. *Bus. Elec.*, 485 U.S. at 740 (Stevens, J., dissenting).

126. *Id.* at 721.

127. *Id.* at 727. Commenting on the significance of the existence of the vertical price

dealer termination on its own had no competitive significance. Justice Scalia's view that RPM is only anticompetitive if it aids cartelization is unduly narrow and ignores how RPM can be anticompetitive when initiated by a powerful manufacturer to foreclose upstream rivals or, more relevant to this case, by a powerful dealer to forestall innovation in distribution and competition by lower-cost and more efficient rival dealers. The record was not clear on whether Business Electronics was more efficient and whether it had free-ridden on Hartwell's sales and promotional efforts.[128] It is thus inconclusive that Hartwell had used the dealer termination to pursue an anticompetitive goal. But there is at least a prima facie case of anticompetitive intent that should not be dismissed out of hand simply because there was no concomitant vertical price fixing agreement. In fact, as pointed out earlier, the lack of a vertical price fixing agreement renders dealer termination more suspicious and more likely to be complaint-motivated. Therefore, the majority was wrong in holding that complaint-motivated dealer termination could not be an antitrust violation without a concomitant vertical price fixing agreement.

Justice Stevens in his dissent shared the same view concerning the possible anticompetitive potential of complaint-motivated dealer termination.[129] He laid out a three-step framework for determining whether dealer termination violates the antitrust law. First, the plaintiff needs to satisfy the hurdle erected by Monsanto to provide "evidence that tends to exclude the possibility that the manufacturer and non[-]terminated distributors were acting independently."[130] Second, the plaintiff must show that the agreement "was based on a purpose to terminate [a dealer] because of its price cutting."[131] Third, the supplier "may rebut the evidence tending to prove that the sole purpose of the agreement was to eliminate a price cutter by offering evidence that it entered the agreement for legitimate, non-price-

fixing agreement, Robinson noted that "[t]he Court in Sharp was also astute in recognizing that even an agreement between supplier and dealer did not necessarily imply an agreement to fix price and hence would not suffice to establish a *per se* violation." Robinson, *supra* note 24, at 598. However, the correct question to ask is not whether dealer termination should be illegal *per se*, which admittedly would be too harsh a rule. Instead, the question should be whether dealer termination should be illegal under certain circumstances, and the answer clearly should be yes. The inquiry was arguably obfuscated during the *per se* rule era because the plaintiff would always seek to link dealer termination to an RPM scheme to take advantage of the *per se* rule. However, Justice Scalia's treatment of the issue is such that it amounts to holding that dealer termination is always legal unless accompanied by a vertical price fixing agreement.

128. *Id.* at 721.
129. *Id.* at 736-758.
130. *Id.* at 753 (quoting *Monsanto*, 465 U.S. at 764).
131. *Id.*

related reasons."[132] This framework represents a good step toward determining the legality of complaint-motivated dealer termination. There are, however, a number of problems with it. First, Justice Stevens again neglected to recognize the right of a supplier under *Colgate* to terminate a dealer for whatever reason, including price cutting, so long as the supplier was not influenced by a complaining dealer to do so. Therefore, it cannot be that termination of a dealer is illegal if it is due to the dealer's price cutting. Dealer termination should only be illegal if it was done at the behest of a complaining dealer to protect that dealer from price competition.

Second, Justice Stevens recited the formula from *Monsanto* for evidence that excludes the possibility of independent action. It is worth parsing out what exactly should be required by this phrase. There are three possibilities. The first possibility is that there was an agreement between the supplier and the complaining dealer to implement an RPM scheme. The second one is that there was an agreement between the supplier and the complaining dealer that the former will terminate the price-cutting dealer, perhaps in exchange for a promise that the latter will continue to carry the former's products. The third one is that the plaintiff is required to show that the supplier was influenced by the complaining dealer in its decision to terminate the price-cutting dealer. Varying degrees of influence can be set for this required showing, ranging from that the dealer complaint was one of the factors contributing to the decision, to that the supplier would not have terminated the price-cutting dealer but for the dealer complaint. Footnote 9 of the *Monsanto* opinion suggests that the Court intended the first formulation.[133] The Court required mutual communication of acquiescence to the price fixing agreement by the supplier and the complaining dealer. This requirement, it has been argued, is counter-intuitive and unduly stringent.

The alternative is an agreement between the supplier and the complaining dealer to terminate the price-cutting dealer. It is important to consider what such an agreement entails and how it is related to the potential anticompetitive effects of the termination. It is somewhat artificial to speak of an agreement on the termination of the price-cutting dealer. This is because there is always an ongoing distribution agreement governing the relationship between the supplier and the complaining dealer. The supplier and the dealer do not enter into separate agreements on resale price maintenance or dealer termination as such. Dealer termination will be one of the items of negotiation between the supplier and the dealer in their ongoing relationship. If the dealer complains to the supplier about price

132. *Id.* at 754.
133. *Monsanto*, 465 U.S. at 764 n.9.

cutting and demands termination of the price-cutting dealer, and the supplier, which otherwise would not have terminated the latter dealer, complied with the complaining dealer's demand, we have all the ingredients of an anticompetitive termination. Requiring proof of an agreement to terminate the price-cutting dealer adds nothing to the analysis.

An agreement usually requires the proverbial meeting of the minds or exchange of promises or commitment. Short of express communication, meeting of the minds is an abstract concept that is easy to describe but hard to prove. Exchange of promises or commitment can be the alternative benchmark. The problem here is that while the supplier will promise to terminate the price-cutting dealer, what the complaining dealer promises in return is often implicit. Unless the complaining dealer explicitly says that it will terminate the relationship if the price-cutting dealer is kept, like what happened in *Business Electronics*, the complaining dealer's reciprocal commitment will be implicit in its continual business relationship with the supplier. The complaining dealer's demand would be more persuasive if backed by a threat to terminate the relationship. But in reality, the dealer can communicate this threat subtly without ever explicitly stating it, especially if the law premises liability on an express exchange of promises. In that case, an exchange of promises or commitment would be very difficult to prove. Requiring proof of an agreement to terminate the price-cutting dealer would erect an unnecessary hurdle for the plaintiff.

This is especially so because the potential for competitive harm from termination of a price-cutting dealer does not depend on the existence of an agreement to terminate that dealer. The removal of a non-free-riding, price-cutting dealer harms intrabrand competition and gives rise to the possibility of a powerful dealer forestalling innovation in distribution and competition from a more efficient rival dealer. If the termination comes from the supplier, it could be explained by a pro-competitive reason or simply the supplier exercising its right to terminate under *Colgate*. But if the termination was motivated by a complaining dealer, the only legitimate reason is if the price-cutting dealer is free-riding. Absent that, a competing dealer has no pro-competitive reason for desiring the termination of a price-cutting rival dealer. Nowhere in this analysis is the presence of an agreement essential or helpful to the reasoning.

The remaining alternative is whether the supplier was influenced by the dealer complaint in its decision. Among the varying degrees of influence that can be required, the but-for standard is the most appropriate. A contributing factor standard would be a significant threat to the supplier's right to terminate a dealer under *Colgate*. It is possible that the supplier would have terminated the dealer anyway and the dealer complaint only gave it the final push. But this termination could very well be illegal under a contributing factor standard. A but-for standard can be satisfied as follows. First, the plaintiff will be asked to show that it was terminated because of a rival dealer's complaint about its price cutting. The plaintiff will be further asked to demonstrate that the complaining dealer is more important to the supplier's business than the price-cutting dealer and thus the supplier would side with the complaining dealer when forced to choose between the two. These two showings establish a prima facie case that the termination was motivated by a dealer complaint and would not have happened without such a complaint. Then the burden shifts to the supplier to show that it had reasons other than dealer complaints to terminate the price-cutting dealer. For example, the supplier can show that the price-cutting dealer was free-riding on other dealers' services. This would provide a legitimate business reason for termination and rebut the prima facie case that the supplier was pressured by the complaining dealer to terminate.

The *Business Electronics* case itself is an apt illustration of a termination that would not have happened but for dealer complaints. Sharp itself tolerated Hartwell's price cutting, which means that it could not have been motivated by Business Electronics' price cutting to terminate it. There were no suggestions that Business Electronics' performance was otherwise not up to standard. It seemed apparent that the sole reason that Sharp terminated Business Electronics was Hartwell's complaint.

11. Leegin Creative Leather Products, Inc. v. PSKS, Inc.

Leegin, of course, had nothing to do with the existence of an agreement in an RPM scheme. It was not about the form of an RPM scheme, but instead about the substance of such schemes.[134] However, the change in the substantive analysis necessitates changes in the formal analysis as well. In a 5-4 decision, the Supreme Court overruled the *per se* rule for RPM that had been in place for ninety-six years since *Dr. Miles*.[135] In the majority opinion, Justice Kennedy acknowledged that RPM can be anticompetitive and pro-competitive, but concluded that "[n]otwithstanding the risks of unlawful conduct, it cannot be stated with any degree of confidence that resale price maintenance 'always or almost always tends to restrict competition and decrease output.'"[136] He further observed that as a *per se* rule "would proscribe a significant amount of procompetitive conduct, these agreements appear ill suited for *per se* condemnation."[137]

An evaluation of the substantive merits of the *Leegin* decision would

134. Leegin Creative Leather Prod., Inc. v. PSKS, Inc., 551 U.S. 877 (2007).
135. *Id.*
136. *Id.* at 894.
137. *Id.*

require a separate article. Suffice it to note for now that the abolition of the *per se* rule for RPM has far-reaching implications on the law on agreement in vertical restraints under *Colgate* and its progeny. At the very least, the sharp distinction drawn by the *Business Electronics* court between vertical price and non-price restraints is no longer justified. This means that dealer termination should no longer be illegal only when undertaken in the context of a vertical price fixing agreement. Dealer termination can be anticompetitive even in the absence of such an agreement.

B. *The Consignment Exception*

The consignment issue is strictly speaking different from the agreement issue discussed above. It is not about when there is an illegal agreement under an RPM scheme. However, the two issues share some important similarities. First, both serve as an exception to the general rule against RPM. Under the agreement issue, if the supplier's conduct falls short of an illegal agreement, there is no illegal RPM scheme. Under the consignment exception, if an arrangement is deemed to be a genuine consignment under *U.S. v. General Electric*, it again will not be deemed an illegal RPM scheme.[138] Both are exceptions based on form that affect the applicability of the substantive rule.

The two leading cases on the consignment exception to the general rule on RPM are *General Electric* and *Simpson v. Union Oil*, which had almost identical facts except that the goods in *General Electric*, the light bulbs, were patented.[139] Yet the cases produced opposite results.[140] In *General Electric*, the company used agents to sell lamps to final customers through a consignment under which the title of the goods never passed to the agents.[141] The agents only bore the costs in storage, transportation, handling, sale, and distribution, held the proceeds of sale on trust for General Electric, and were required to return all the unsold lamp within a certain period of time.[142] The Supreme Court held that these were genuine agents who were selling lamps on consignment from General Electric.[143] The Court focused on a number of factors, including the fact that General Electric retained ownership of the lamp, which was passed on directly to the final customers, that the agents

138. United States v. Gen. Elec. Co., 272 U.S. 476 (1926) (holding that genuine contracts of agency are not violations of the Sherman Act, however widespread they may be).

139. *Id.* at 479.

140. *Id.*; Simpson v. Union Oil Co. of Cal., 377 U.S. 13 (1964) (holding that maintaining gasoline prices through a coercive consignment agreement between a company and station operator was illegal under antitrust laws).

141. *Gen. Elec.*, 272 U.S. at 484.

142. *Id.* at 481-82.

143. *Id.* at 484.

had no obligation to pay General Electric until the lamps were sold to final customers, and that the agents had no right to deal with the lamps in any way inconsistent with General Electric's ownership.[144] The Court further noted that the fact that the agents were responsible for loss or damage to the goods and for the various operational expenses was not inconsistent with a genuine agency model.[145]

In *Simpson*, Union Oil distributed its oil to retail customers under a consignment system under which agents signed one-year leases with Union Oil.[146] The leases would be terminated if the agent did not follow the prices prescribed by the company.[147] Like in *General Electric*, title to the oil remained with Union Oil until it was sold to final customers.[148] The agents were similarly responsible for losses of the consigned gasoline in his possession and for personal liability and property damage insurance.[149] Furthermore, the agent bore all the costs of operation and was compensated on a commission basis.[150] The Court held that the consignment system was an illegal RPM scheme on a number of grounds.[151] First, the Court noted that the lease system was used in a coercive manner to compel the agents to follow the prices prescribed by Union Oil.[152] The Court compared the lease system to the techniques used by the defendant in *Parke, Davis* and observed that it was equally if not more effective than those techniques.[153] Second, the Court stated that the system covered a vast gasoline distribution system and fixed the retail prices of many retail outlets.[154] Third, the Court noted that the agents bore all the risks of operation but yet had no control over the most important parameter affecting the profitability of their businesses.[155] Unsurprisingly, Union Oil attempted to rely on *General Electric* to salvage its case.[156] The Court rejected the reliance on *General Electric* on the grounds that the goods in *General Electric* were patented, even though the *General Electric* court placed no emphasis on that fact in upholding the consignment system.[157]

In light of these conflicting precedents, the task of drawing the line

144. *Id.*
145. *Id.*
146. *Simpson*, 377 U.S. at 14.
147. *Id.* at 14-15.
148. *Id.* at 15.
149. *Id.*
150. *Id.*
151. *Id.* at 17-21.
152. *Id.* at 17.
153. *Id.*
154. *Id.* at 21-22.
155. *Id.* at 20-21.
156. *Id.* at 22-23.
157. *Id.* at 23.

between permissible use of a consignment system to control resale prices and an illegal RPM scheme has been largely left to the lower courts, which have generally focused on the independence of the agents from the supplier.[158] Commentators have argued that it is exceedingly difficult to distinguish *General Electric* and *Simpson*, and that it has been generally assumed that *Simpson* has implicitly rejected *General Electric*.[159] Despite this view and the government's successful challenge of the General Electric consignment system in a 1973 action following *Simpson*[160], lower courts have continued to uphold the use of bona fide consignment system to establish resale prices.[161] The wisdom of the consignment exception has been called into question. Harrison argued that "the use of agents or consignees may not involve a resale but they are still agreements and may be anticompetitive."[162] One may defend the exception on the ground that if the supplier has never parted with title to the goods, it should retain the right to set the resale price

158. Harrison, *supra* note 92, at 1150.

159. Calvani & Berg, *supra* note 9, at 1178.

160. United States v. Gen. Elec., 358 F. Supp. 731 (S.D.N.Y. 1973).

161. *See* Valuepest.com of Charlotte, Inc. v. Bayer Corp., 561 F.3d 282 (4th Cir. 2009) (holding that RPM arrangement was legal because a genuine agency relationship existed between the distributors and manufacturers which bore the economic risks of distribution); Day v. Taylor, 400 F.3d 1272 (11th Cir. 2005) (holding that relationships between moving equipment rental company and independent dealers were genuine agencies and thus the RPM provisions therein were legal); Ryko Mfg. Co. v. Eden Serv., 823 F.2d 1215 (8th Cir. 1987) (finding that manufacturer's national account program did not constitute an illegal resale price maintenance scheme because distributor did not act as a separate business entity bearing independent economic risks of independent commercial transactions); Hardwick v. Nu-Way Oil Co., Inc., 589 F.2d 806 (5th Cir. 1979) (holding that the oil company's retention of the sole right to set price of gasoline at the pump did not constitute illegal price fixing under antitrust laws because the station operator had no independent authority to set prices or control sales and few managements rights regarding the business); Pogue v. Int'l Indus., Inc., 524 F.2d 342 (6th Cir. 1975) (finding no illegal vertical price-fixing because plaintiff sold merchandise only on consignment and defendant maintained dominion and control over merchandise); Agrashell, Inc. v. Hammons Prod. Co., 479 F.2d 269 (8th Cir. 1973) (holding that exemption for RPM provisions under *General Electric* applies to agency agreements, but ends when the patent expires); North Am. Prod. Corp. v. Nick Penachio, Inc., 705 F. Supp. 746 (E.D.N.Y. 1988) (holding that fresh produce distributor could not establish a claim for vertical price restraint because it was an agent and not an independent distributor of the wholesale supplier); Illinois Corp. Travel, Inc. v. Am. Airlines, Inc., 700 F. Supp. 1485 (N.D. Ill. 1988) (finding that any price-fixing agreement between the travel agency and the airline was legal because agency was airline's true agent); Everhart v. United Refining Co., No. C79-1555-Y, 1980 WL 1993 (N.D. Ohio Dec. 16, 1980) (granting summary judgment for defendant denying antitrust claim because the plaintiff was an employee and not an independent contractor and thus RPM provision benefited from the *General Electric* exception). *But see* Greene v. Gen. Foods Corp., 517 F.2d 635 (5th Cir. 1975) (holding that the MFSA system constituted a vertical price-fixing violation of the Sherman Act because retailers were independent distributors which bore economic risks).

162. Harrison, *supra* note 92, at 1148.

of its own goods. After all, one should have the right to choose how one disposes of one's own property. This argument, which is premised on a distinction between sale and non-sale transaction, was however firmly rejected by the Supreme Court in *GTE Sylvania*.[163] The *Sylvania* court noted that "[n]or is there even an assertion in the [*Schwinn*] opinion that the competitive impact of vertical restrictions is significantly affected by the form of transaction."[164] This observation seems to be equally applicable to a regular RPM scheme and one implemented through a consignment system.

II. JUSTIFICATIONS FOR THE AGREEMENT REQUIREMENT IN VERTICAL RESTRAINTS

Before exploring whether an agreement is necessary for establishing a vertical restraint, it is important to define an agreement. In the context of horizontal agreements, Kaplow defined an agreement as "a harmony of opinion, action, or character."[165] He further explained that "[a] harmony of opinion exists when there is a meeting of the minds"[166], a phrase which appears frequently in the discourse on the notion of agreement, especially horizontal agreements.[167] The Supreme Court imported this concept into the realm of vertical restraints in *Monsanto*, holding that to prove the existence of a vertical price fixing agreement after dealer termination, the plaintiff must adduce evidence that indicates "a unity of purpose or a common design and understanding, or a meeting of minds in an unlawful arrangement."[168] Kaplow described meeting of the minds as "a metaphorical phrase that directs attention to parties' subjective states."[169] By adopting this metaphorical phrase, the concept of agreement focuses not on the parties' action, but on their subjective state of mind, which may entail examination of issues such as what the parties were thinking at the time of the agreement, their motives for entering into the agreement, and how willing they were to enter into the agreement. Much of the discourse on agreement has taken place in the horizontal context. It turns out that there are substantial differences in the role played by the concept of agreement in the horizontal and the vertical contexts such that the horizontal approach to agreement may not be suitable for and directly transposable to the vertical context.

163. *GTE Sylvania, Inc.*, 433 U.S. at 54.
164. *Id.*
165. Louis Kaplow, *On the Meaning of Horizontal Agreements in Competition Law*, 99 CAL. L REV. 683, 705 (2011).
166. *Id*.
167. *See* American Tobacco Co. v. U.S., 328 U.S. 781, 810 (1946) (using the phrase to characterize a horizontal conspiracy).
168. *Monsanto*, 465 U.S. at 764 (quoting *Am. Tobacco Co.*, 328 U.S. at 783).
169. Kaplow, *supra* note 165, at 707.

A. *Purpose of the Agreement Requirement*

Why does antitrust law attach so much importance to the concept of agreement in the application of Section 1? The simplest answer is that it is a statutory requirement. Section 1 states that "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal."[170] Courts have encapsulated the concepts of contract, combination, and conspiracy in the overarching notion of agreement and deemed an agreement to be a prerequisite for the application of Section 1.[171] This of course does not answer the question. The fact that an agreement is required by the statutory language does not indicate what purpose the concept is supposed to serve, which in turn affects how it should be crafted and applied.

The requirement of an agreement may serve a number of purposes. First, it may be used to draw the boundary between multilateral conduct and unilateral conduct. Section 1 does not prohibit unilateral conduct and only forbids conduct involving more than one party. One justification for distinguishing multilateral conduct from unilateral conduct is that "conduct of a single firm is less threatening than that engaged in by a collective."[172] While this assertion has a great deal of intuitive appeal and is a widely-accepted mantra in antitrust law, upon deeper reflection, it is unclear why it is so. What determines the quantum of competitive harm that can be inflicted by particular conduct is the degree of market power wielded by the party or parties involved. It cannot be true that a single firm with 90% market share is capable of less competitive harm than ten firms each possessing 2% market share. Therefore, it cannot be categorically asserted that concerted action is inherently more anticompetitive than unilateral conduct.

Even if it was accepted that concerted action is more dangerous than unilateral conduct, an agreement would not be necessary to allow the parties to pool together their market power. If parties act in the same manner against the same firms or customers, their conduct will produce the same effect regardless of whether they have an agreement or not, however an agreement is defined. If, for whatever reason (some of which will be addressed subsequently), it is decided that it is important to distinguish between deliberate pooling of market power and mere parallel conduct, this concern is much more relevant in the horizontal context as opposed to the vertical context.

170. 15 U.S.C. § 1 (2012).

171. Lawrence A. Sullivan & Warren S. Grimes, THE LAW OF ANTITRUST: AN INTEGRATED HANDBOOK § 5.2 (2000).

172. *Id.*

While there is aggregation of market power in the horizontal context,[173] — and it may be necessary to distinguish between problematic and permissible aggregation — vertical restraints do not result in the pooling of market power. In fact, Judge Posner characterized vertical restraints as "unilateral abuses of market power."[174] Without an aggregation of market power, the need to distinguish between problematic and permissible aggregation disappears. Furthermore, the need to distinguish between multilateral and unilateral conduct in the vertical context is much less urgent. The notion of agreement hence plays a much less important role in vertical restraints.

The second possible purpose to be served by the agreement requirement is to determine the extent of voluntariness in the parties' actions. This is one of the issues that follows from focusing on the parties' subjective minds. Based on Kaplow's definition of agreement as harmony of opinion, action, or character, one would assume that an agreement represents voluntary assent to the joint enterprise. This is probably true in the context of horizontal agreements. Except for extreme scenarios in which a firm is coerced into joining a cartel by more powerful firms in the market, most horizontal agreements are fully voluntary. Therefore, the degree of voluntariness is usually not an issue in horizontal restraint cases. Voluntary assent, however, cannot be taken for granted in vertical restraints.[175]

The simple reason is that while the supplier's interest and the dealer's interest may not fully align, an agreement may nonetheless be formed because of one party's reliance on the business relationship.[176] In the RPM

173. *See* Burns, *supra* note 61, at 11 (stating that horizontal arrangements combine otherwise competing firms' market power, while vertical arrangements do not increase market power); Correia, *supra* note 53, at 210 ("Horizontal agreements may create market power by allowing firms acting jointly to raise prices over competitive levels when a single firm cannot. This ability to create market power through agreements among competitors is the basis of the concern about horizontal agreements generally."); Hovenkamp, *supra* note 24, at 1 ("[H]orizontal agreements concern us because they may create market power that did not previously exist. The ordinary cartel agreement creates market power by consolidating the price [and] output choices of firms that otherwise lack power over output or price.").

174. Richard A. Posner, *Vertical Restraints and Antitrust Policy*, 72 U. CHI. L. REV. 229, 229 (2005).

175. *See* Burns, *supra* note 61, at 13-14 (stating that while horizontal agreements generally involve a common plan for the common benefit of the participating firms, vertical agreements do not necessarily include such unity of purpose and may even be undesirable for dealers upon whom manufacturers place restraints); Calvani & Berg, *supra* note 9, at 1165-66 (stating that in the horizontal context, competitors acting in concert have a common economic interest, while in the vertical context, the economic interests of manufacturers and vendors may conflict).

176. *See* Burns, *supra* note 61, at 14-15 (identifying three scenarios within manufacturer-imposed vertical restraints in which a dealer could be pleased, indifferent, or opposed to the restraints but still must participate in the agreement because of its reliance on the

context, a dealer may disagree with a minimum resale price because it wishes to be a no-frills price cutter. A dealer may disagree with the minimum resale price because it believes that the price is set too low and estimates that a higher level of service than is supported by the current minimum resale price would attract more customers and increase sales.

A dealer may also disagree with an RPM scheme because it is used to facilitate a manufacturer cartel. If the dealer level of the market is competitive, the dealers will only earn a competitive return, and the supra-competitive profit generated by the cartel will only go to the suppliers or manufacturers. In the meantime, the upstream cartel will reduce downstream sales and hence dealer revenue.[177] Conversely, the dealers may organize a cartel and require a supplier or manufacturer to police it through an RPM scheme. The supplier will be hurt by this cartel as downstream sales will fall as a result of the cartel. If the supplier can only charge a competitive wholesale price and does not get to share the profit from the dealer cartel, the supplier will be worse off and will oppose the RPM scheme.[178]

In the horizontal context, when the interests of the two parties are not aligned, there will be no joint enterprise. In the vertical context, however, an agreement could still be formed despite the partial misalignment of interests. Parties to a vertical agreement may need each other's business so much that the gains from a continual trading relationship outweigh the loss from the misaligned interests. For instance, a dealer may determine that reduced sales as a result of a manufacturer cartel are still better than no sales from that manufacturer. Or a supplier may decide that reduced upstream sales as a result of a dealer cartel are better than no sales at all if it abandons all dealers. Due to the multitude of financial considerations which may go in opposite directions in the vertical context, an agreement does not mean that there is full, voluntary assent. A party may have accepted a vertical agreement grudgingly.

The foregoing discussion is particularly relevant to the coercion theory of agreement. It suggests the futility of inquiring into the degree of coercion to which the party is subject to. Unless there is complete alignment of interests between the supplier and the dealer in the use of RPM, or at least indifference to its use, there is always a degree of coercion involved in a party's participation in an RPM scheme. Therefore, if the search for an agreement is meant to determine the extent to which the parties consent to the RPM scheme voluntarily, the exercise is likely to be a pointless one. An inquiry into the degree of coercion would be fruitful if it provided useful information on the competitive effects of the RPM scheme. There is,

manufacturer).

177. *Id.* at 15-16.

178. *Id.*

however, unlikely to be a direct correlation between the competitive harm of an RPM scheme and the degree of coercion involved.

Coercive measures may be necessary to secure compliance when the counterparty resists. Assuming that it is a supplier-imposed RPM scheme, the supplier will implement coercive measures when the dealer refuses to abide by the RPM scheme. This will happen when the two parties have similar levels of bargaining power, their economic interests with respect to the RPM scheme diverge, and the supplier's threat to terminate a non-compliant dealer for some reason lacks credibility, which causes the dealer to test the waters by resisting. Therefore, the degree of coercion reflects the parties' relative bargaining power, the extent to which the parties' interests coincide, and the credibility of the threat to terminate the relationship. The question is whether any of these factors shed light on the competitive effects of an RPM scheme.

A supplier may have a great deal of bargaining power because it has substantial market power in the market or because its product is a must-carry product for the dealers. A dealer may wield substantial bargaining power because it is a prominent retailer with substantial market share or it is a quality-certifying retailer which is particularly important to a supplier selling high quality products.[179] All this information may be relevant to the analysis of the likely competitive effects of an RPM scheme. However, as opposed to trying to deduce such information indirectly from the degree of coercion, it would be much more straightforward to extract the information directly and apply it in the competitive effects analysis.

There is no clear correlation between the alignment of the parties' interests and the likelihood of competitive harm of an RPM scheme. It would seem that when RPM is used to facilitate a cartel, either at the supplier or the dealer level, supplier and dealer interests would clash. Cartelization at one level would almost always reduce sales at the other level. Meanwhile, if an RPM scheme is used by a powerful supplier or dealer to foreclose rivals, the counterparty would need to be sufficiently compensated so that it is worth its while to take part in the foreclosure strategy. In that case, supplier and dealer interests would likely be aligned. There is similarly no discernible pattern in the alignment of the parties' interests when an RPM scheme is used pro-competitively. For instance, when an RPM scheme is used to prevent free riding or to certify quality, there are always some dealers that agree with the supplier and some price- cutting dealers that do not. Therefore, the alignment of the parties' interests is not a useful indicator of

179. *See* Howard P. Marvel & Stephen McCafferty, *Resale Price Maintenance and Quality Certification*, 15(3) RAND J. ECON. 346 (1984) (arguing that RPM can be used in a procompetitive manner by preventing free-riding of a quality certifying retailer by other low-cost retailers).

the competitive effects of an RPM scheme.

The credibility of the threat to terminate depends on a range of factors, one of which is the clarity and firmness with which the consequence of non-compliance has been communicated to the counterparty.[180] If a supplier has made it firm and clear that it will terminate a non-compliant dealer immediately and the supplier's product is important to the dealer, it will require not much coercion on the part of the supplier to secure compliance. The clarity of communication between the parties, however, tells us nothing useful about the likely competitive effects of an RPM scheme.

The degree of voluntary participation in a joint enterprise could serve one function: to determine the degree of relative culpability of the parties. In *Perma Life Mufflers, Inc. v. International Parts Corp.*, the Supreme Court was confronted with the issue of whether the defendant's franchisees were barred by the common law defense of *in pari delicto* from suing the supplier over a range of allegedly illegal vertical restraints imposed by the supplier.[181] The concurring justices expressed a range of views on the extent to which relative culpability should bar recovery under antitrust law.[182] Justice Fortas argued that a fellow member of a collusive scheme should not be allowed to "sue the other for discriminatory or restrictive practices which allegedly diminished its take from the enterprise."[183] Justice Marshall argued, "[W]here a defendant in a private antitrust suit can show that the plaintiff actively participated in the formation and implementation of an illegal scheme, and is substantially equally at fault, the plaintiff should be barred from imposing liability on the defendant."[184] The majority, however, seemed to have gone further than the concurring justices and proclaimed, "[N]othing in the language of the antitrust acts [] indicates that Congress wanted to make the common-law *in pari delicto* doctrine a defense to treble-damage actions[.]"[185] In the remainder of the opinion, the Court seemed to have softened its stance and merely asserted that the plaintiffs should not be denied recovery "merely because they have participated to the extent of utilizing illegal arrangements formulated and carried out by others."[186] The Court proceeded to explain how the vertical restraints imposed in the case were against the franchisees' interests and note that they only accepted these restraints to maintain their business relationship with the defendant.[187]

180. It also depends on the extent to which the party can do without the counterparty, which ties back to some of the issues addressed under bargaining power.
181. Perma Life Mufflers, Inc. v. Int'l Parts Corp. 392 U.S. 134, 135 (1968).
182. *Id.* at 138-147.
183. *Id.* at 147.
184. *Id.* at 149.
185. *Id.* at 138.
186. *Id.* at 139.
187. *Id.*

The lack of clarity concerning the precise scope of the holding notwithstanding, it is clear that the degree of voluntary participation should be a relevant consideration in determining the relative culpability of the parties. It is difficult to dispute Justice Marshall's view that a party that is equally at fault in the illegal scheme should not be allowed to recover from a fellow wrongdoer. This, however, does not justify the imposition of an agreement requirement in every vertical restraint case. The inquiry into agreement is not undertaken to determine relative culpability; it is done to decide whether a vertical restraint has been put in place. In most vertical restraint cases, the issue of the plaintiff's culpability does not arise. There is no need to impose an agreement requirement in the vast majority of cases in which relative culpability is irrelevant. Encapsulating the relative culpability inquiry in the agreement requirement is also logically questionable. The fact that a party is much more at fault for the wrongdoing than the other party does not mean that a wrongdoing does not exist. Therefore, the need to determine relative culpability does not justify an inquiry into the degree of voluntary participation under the rubric of the existence of an agreement.

The third possible purpose to be served by the requirement of an agreement is to locate conduct that is subject to possible antitrust condemnation. This suggests that the usual mode of analysis would be first to identify the existence of an agreement that may raise antitrust concerns and then to apply substantive analysis to determine the competitive effects of the conduct. In reality, however, the existence of an agreement usually only matters when substantive harm has been observed and the question is whether it is produced by the proscribed conduct. Therefore, the existence of an agreement is usually critical only when a particular outcome that is consistent with *per se* illegal conduct has been observed. It is seldom a pivotal issue when the conduct is subject to the rule of reason because whether particular conduct took place does not immediately determine legality. The agreement requirement is hence especially relevant in the horizontal context, where it is important to determine whether collusion exists from the observation of parallel pricing behavior.

Courts and commentators have generally concurred that as a matter of substantive antitrust policy, parallel conduct by multiple parties does not run afoul of the law absent an agreement showing that the parties were acting with a common purpose or striving to achieve a common goal.[188] Hence,

188. A number of reasons inform this view, including the fact that price uniformity can be the result of both intense competition and collusion and the practical difficulties in crafting remedies. *But see* Kaplow, *supra* note 165, at 809-14 (raising theoretical objections against allowing parallel conduct of multiple parties in case of no apparent agreement); Louis Kaplow, *An Economic Approach to Price Fixing*, 77 ANTITRUST L.J. 343, 346 (2011) (arguing that the harms of horizontal price fixing should be addressed by focusing on the extent and

when a firm raises price in response to a competitor's price increase, the law needs to determine whether it does so pursuant to a common understanding with its competitor or only in accordance with its independent judgment about changes in market dynamics. This is especially the case because the *per se* rule applies to horizontal price fixing. The legality of parallel pricing behavior hinges on whether it is done with a common purpose or pursuant to a common scheme. Once it is found that the defendants have agreed to fix prices, the inquiry ends. Thus, the concept of agreement serves an important purpose in the horizontal context.

The concept of agreement does not serve the same purpose in the vertical context.[189] There is no need to distinguish between consciously parallel pricing behavior from deliberate concerted price increase. When a dealer charges the minimum prices demanded by the supplier, there is no question that the dealer does so at the behest of the supplier, regardless of whether there is express communication between the parties or whether the result was accomplished solely through unilateral announcements. The dealer is responding to the supplier's demand and not reacting to changes in market dynamics upon exercising its own independent judgment. A firm raising its price is part of the normal operation of the market and may not be an invitation to collude or part of a collusive scheme. When a supplier demands a dealer to conform to minimum resale prices, there is no ambiguity as to what the supplier wants the dealer to do. Nor is it part of normal market operation. It would be very difficult for antitrust law to prohibit a firm from raising or adjusting its prices and its competitor from responding to it. The same difficulty is absent if the antitrust law wants to prohibit any attempt to impose an RPM scheme, either through unilateral announcements or concerted action.

The one plausible argument in defense of drawing a distinction between unilaterally imposed and concerted RPM schemes is the preservation of trader freedom, which is the argument made by the Supreme Court in *Colgate*.[190] However, the invocation and endorsement of the trader freedom argument in the RPM context and its rejection elsewhere in antitrust, such as cartel conduct and monopolization, is arbitrary and incapable of a principled justification. Robinson argues:

> [I]t is the central purpose of antitrust law to interfere with trader

duration of the pricing, not on the means of achieving the price).

189. Commentators have noted that the concept of agreement serves different purposes in the horizontal and the vertical restraint contexts. Burns, *supra* note 61, at 3 ("[T]he Court has unthinkingly transplanted the language and learning of horizontal agreements into the vertical context, with the result being that the Court's rationale for scrutinizing vertical restraints is now at odds with the law of vertical agreements."); Robinson, *supra* note 24, at 597.

190. United States v. Colgate Co., 250 U.S. 300 (1919).

> freedom where it causes social harm; any distinction between unilateral and concerted action-'agreement' in the broadest sense of that term-must depend, therefore, on an assessment that the two types of action have different consequences rather than on notions of mercantile freedom.[191]

In short, the agreement requirement cannot be justified solely on the basis of boundary setting between permissible and illegal conduct divorced from substantive policy considerations.

When the *per se* rule applies to particular conduct, it is perhaps inevitable that the concept will be laden with substantive content. After all, we are trying to conduct the formal and the substantive analysis simultaneously. When the rule of reason applies, however, there is no reason for the agreement requirement to be used as a proxy for substantive analysis. The substantive analysis can be conducted after the formal identification. The separation of formal identification and substantive analysis means that the sole purpose of the concept of agreement is to serve as an identification device — to identify situations in which the substantive issues may arise. If two different forms of conduct may produce the same effect, the identification device should identify both as candidates for further examination. The legality of particular conduct can no longer be premised on such a formal concept as the existence of agreement. It must be determined with reference to substantive antitrust considerations, i.e., whether the conduct creates consumer harm. Antitrust has always been about substance, not form. Formal devices cannot be applied in such a way that they obscure substantive policy objectives of antitrust. This is especially true for vertical restraints. Robinson notes, "The existence or nonexistence of a vertical agreement is altogether irrelevant to the kind of public injury that the antitrust laws are designed to prevent."[192]

To sum up, the agreement requirement cannot be justified by the need to distinguish between multilateral and unilateral conduct in the vertical context because of the absence of aggregation of market power in vertical restraints. It also cannot be justified as a tool to assess the degree of coercion in an RPM scheme because absent complete alignment of the parties' interests, there is always some degree of coercion in every RPM scheme and because the degree of coercion is not an accurate indicator of competitive harm. The appropriate purpose of the agreement requirement is to serve as a device for identifying the locus of possible competitive harm. However, the identification of an agreement is much less important in the vertical context where the rule of reason applies across the board after *Leegin*. Given

191. Robinson, *supra* note 24, at 581.
192. *Id.* at 581.

that the competitive effects of particular conduct will be assessed after substantive analysis, the concept of agreement should no longer draw arbitrary distinctions between situations that produce the same substantive effects. If unilaterally imposed and mutually agreed RPM schemes produce the same substantive effects, they should be treated similarly by the formal identification device.

B. *Evidentiary Issues*

There are some evidentiary issues concerning the proof of an agreement in the vertical context. The first is the question of which agreement counts. One major difference between horizontal restraints and vertical restraints is that it is not necessary for competitors to enter into agreements with each other in order for markets to operate. If the agreement is a bona fide cooperative agreement between competitors, such as a joint venture, the issue of agreement usually does not arise. There is no question that the parties have agreed to start a collective venture. If the agreement were a cartel agreement, then the discovery of any agreement between them would result in condemnation. Thus, in the horizontal context, when the existence of an agreement is an issue, the proof of an agreement usually determines liability. In the vertical context, under the *Colgate* doctrine, the issue of agreement arises against the backdrop of a supply agreement between the supplier and the dealer. As Professor Hovenkamp has argued, if one were to apply the approach to cartel agreements in the vertical context, it would amount to the evisceration of the agreement requirement.[193] By definition, an agreement must exist in the vertical context. Therefore, the plaintiff would need to show not only that there is an agreement between the supplier and the dealer, but that there is an agreement that would attract liability.[194] If the alleged conduct was RPM, the plaintiff would need to show that the supplier and the dealer agree to set minimum resale prices. What complicates matters is the fact that there is likely to be regular communication between the supplier and the dealer over a variety of issues, and they share the common goal of increasing sales of the product.[195]

The task of identifying the agreement that attracts liability is made more difficult by the fact that the Supreme Court has been rather cavalier about which agreement counts for the purpose of liability.[196] The Court's approach

193. Hovenkamp, *supra* note 24, at 2.

194. Burns, *supra* note 61, at 10.

195. Correia, *supra* note 53, at 190.

196. Hovenkamp, *supra* note 24, at 12 ("A curiosity of many dealer-complaint cases is their failure to identify the nature and content of the alleged complainer-manufacturer agreement."); Correia, *supra* note 53, at 199 (noting that the *Monsanto* court failed to

to the identification of agreement can be categorized into two situations: direct proof of an RPM agreement and inference by dealer termination. In the direct proof situation, the Court has resorted to the following: an agreement to fix resale prices either with the non-compliant dealer[197] or the compliant dealers; an agreement with third parties, including wholesalers and third-party agents, to enforce an RPM scheme;[198] an agreement with wholesalers and dealers to report on non-compliant dealers;[199] and even an agreement with the customers of a non-compliant dealer.[200]

In the dealer termination context, the Court has examined the possibility of an agreement with a complaining dealer to terminate a non-compliant dealer,[201] and an agreement to fix resale prices in conjunction with an agreement to terminate a non-compliant dealer.[202] It was argued earlier that in the context of dealer termination, it is unnecessary to identify an agreement between the supplier and a complaining dealer to terminate the non-compliant dealer or an RPM agreement between the supplier and the complaining dealer. The focus should be on whether the supplier would have terminated the non-compliant dealer but for dealer complaints. As for the direct proof context, one cannot help but feel that there is a degree of artificiality in premising liability for resale price maintenance on the agreements between the supplier and various parties to enforce the RPM scheme. It is almost as if the Court has observed the result of uniform resale prices and sets about looking for an agreement, any possible agreement, within the RPM scheme to satisfy the agreement requirement for liability. If the purpose of the agreement requirement is to identify the locus for competitive harm, however, these agreements with third parties to enforce the RPM scheme should not matter.

One way to rationalize the Court's use of these agreements to establish liability is to deem an agreement to enforce an RPM as circumstantial evidence from which one can infer the existence of an agreement to fix resale prices. The probative value of these agreements, however, is likely to be limited. Evidence of enforcement mechanisms indicates the existence of an RPM scheme; otherwise, there would be nothing to enforce. However, it does not tell us whether the scheme was the result of an illegal agreement or a unilaterally announced policy. One may argue that enforcement mechanisms would need to be more elaborate in the latter case because if the

articulate the precise agreement at issue).

197. *See Albrecht*, 390 U.S. at 163 (occurring at the moment the non-compliant dealer capitulates and complies with the supplier's demand.).

198. *Albrecht*, 390 U.S. at 163; *Parke, Davis & Co.*, 362 U.S. at 45.

199. *Beech-Nut Packing*, 257 U.S. at 446.

200. *Albrecht*, 390 U.S. at 163.

201. *Bus. Elec. Corp.*, 485 U.S. at 722.

202. *Id.* at 726-27.

dealers had agreed to the scheme in the first place, they were more likely to comply with it, resulting in less need for active policing. That would be true if the RPM scheme were equally in the dealers' interests as the supplier's interest. But as was previously discussed, it need not be true. It is important to bear in mind the prisoner's dilemma facing dealers. The dealers have great incentive to cheat because if every other dealer but himself abided by the RPM scheme, he would stand to profit handsomely. Therefore, an enforcement mechanism would be necessary even for an RPM scheme produced by an agreement.

In any case, even if it were accepted that a unilaterally imposed RPM scheme required more active enforcement, it would be very difficult to determine the appropriate threshold for such enforcement. The answer is likely to be so case-specific that using an agreement to enforce an RPM as circumstantial evidence is unlikely to be a fruitful endeavor. Therefore, if identification of an agreement were to be a meaningful exercise, it should be the RPM scheme itself that should be the subject of identification, not other ancillary agreements. Obviously, all this confusion concerning what is the appropriate agreement to be used to satisfy the agreement requirement would be obviated if one no longer insisted on an agreement in RPM cases.

Another evidentiary issue is the relevance of parallel conduct. This issue carries over from the horizontal context, within which one of the central issues for the agreement requirement is to what extent one can infer an agreement from parallel conduct.[203] In the vertical context, the parallel conduct spoken of is usually dealer complaints and termination by the supplier. By the same logic, it may be tempting to conclude that parallel conduct on its own should not constitute a vertical agreement, as some commentators have argued.[204] It is worth pointing out, however, that parallel conduct is a bit of a misnomer in the vertical context. In the horizontal context, two competitors charge the same price or raise the price by the same amount; their conduct is literally parallel. In the vertical context, the supplier and the dealer do not undertake parallel conduct. Only the supplier can terminate the non-compliant dealer; the complaining dealer cannot. Therefore, the most that can be said about the situation is that there is parallel intention or preference on the part of both the supplier and the complaining dealer as they desire the same outcome: the termination of the non-compliant dealer.

If an agreement is interpreted as a meeting of the minds, it admittedly can be a bit of a stretch to infer an agreement from parallel conduct. The same conduct may be motivated by different intentions or the same intention

203. Floyd, *supra* note 18, at 279.
204. *Id.*

arrived at independently. However, in the vertical "parallel conduct" scenario, we know that both parties desire the same outcome. They both want the non-compliant dealer terminated.[205] Yet in the vertical context, not only do we demand common intentions among the parties to establish an agreement, we also demand common motivations. We require that the supplier and the complaining dealer desire the same outcome for the same reason. They both want to terminate the price-cutting dealer, not because he was free-riding, but because they want to shield the complaining dealer from legitimate price competition. In other words, they want to terminate the price-cutting dealer for an anticompetitive reason. This heightened requirement is a concession to the fact that, in the context of RPM, the same intention can be motivated by an anticompetitive or a pro-competitive reason. And we do not want to penalize a supplier for wanting to terminate a free-riding dealer.

A number of comments are in order. First, this is another example of substantive considerations seeping into a formal definition issue.[206] When the *per se* rule applied to RPM, there was no proper analysis of the substantive issues. There was no proper consideration of whether the RPM scheme was justified by prevention of free-riding. Therefore, the Court indirectly incorporated this analysis in the agreement issue. However, the agreement issue is not the proper place for considering the applicability of a substantive defense, especially when full analysis of it is now possible under the rule of reason. It is therefore questionable whether the heightened requirement of common motivation is still justified. Second, even if this requirement were to be retained, it should only apply to situations in which free riding is plausible. It has been pointed out that for many goods and services subject to RPM, there is no sales or after-sales service to speak of.[207] In the absence of such service, there is no free riding concern. A stricter definition of agreement that aims to distinguish between anticompetitive and pro-competitive dealer termination would no longer be justified.

Third, if an agreement is interpreted as a meeting of the minds, then common intentions should indicate an agreement. This means that every time a dealer complains about another dealer and the supplier agrees with the complaining dealer and terminates the non-compliant dealer, there would be an agreement. This basically would cover every dealer termination scenario.

205. *Id.* at 278

206. *See* Hovenkamp, *supra* note 24, at 5 (explaining that the court must first define its concept of an agreement before analyzing questions of motive).

207. *See* Marina Lao, *Resale Price Maintenance: A Reassessment of its Competitive Harms and Benefits*, *in* MORE COMMON GROUND FOR INTERNATIONAL COMPETITION LAW? 59, 75, 80 (Josef Drexl et al. eds., 2011) (explaining that the market provides a wide array of options, one of which includes low-service stores, which provide little retail service, to suit customers' price and service needs).

This may raise concerns because it may be feared that it would open floodgates to dealer termination suits, which the Supreme Court was so eager to control in *Monsanto* and *Business Electronics*. This concern, however, is overblown because the fact that an agreement is found in every dealer termination situation does not mean that every instance of dealer termination is illegal. The substantive analysis that is removed from the formal issue of agreement can be reincorporated in a later stage to consider the competitive effects of dealer termination. It is here where the justification of dealer termination, such as the prevention of free riding, is considered. As argued earlier, if the supplier can prove that its termination decision was motivated by free riding concerns, the plaintiff will have failed to satisfy the but-for standard in the proposed analytical framework for dealer termination cases.

Eschewing the requirement of common motivations helps to remove an artificial barrier to dealer termination suits, which presently require a plaintiff to show that the termination was motivated by an improper reason — either by showing there is a separate vertical price fixing agreement or other means — when it is possible that no plausible claims of free riding can be made. Instead, in the substantive analysis stage, once the plaintiff has shown that he was terminated due to his price-cutting and that the complaining dealer's business is more important to the supplier than the non-compliant dealer's business, the burden shifts back to the defendant to justify the termination by alternative reasons.

Parallel conduct is not confined to dealer termination. It is also found in the initial establishment of an RPM scheme through unilateral announcements of policy. When a supplier announces the minimum resale prices it wishes its dealers to charge and the dealers comply, one may characterize it as parallel conduct. This is subject to the same qualification that it is not the conduct that is parallel — the supplier and the dealers did not undertake the same action — but the intention that is parallel. They both share the intention to put in place an RPM scheme under which every dealer would charge the minimum resale prices. Under the *Colgate* doctrine, this common intention would not constitute an agreement. Again, we need to know that the common intention is motivated by the same motive. Professor Hovenkamp argued that "[i]f unilateral termination of a price cutter because of price cutting does not constitute an agreement, then no agreement exists unless there is a motive for and evidence of the manufacturer's agreement with some third party."[208] He further argued that the notion of motive cannot be considered in the abstract: "[A] motive to affect resale prices (1) is not meaningful unless we distinguish resale price control as such from preventing free riding on important services provided by other

208. Hovenkamp, *supra* note 24, at 5.

dealers . . . ."[209] In other words, Professor Hovenkamp advocated the incorporation of substantive analysis into the definition of an agreement in the initial RPM agreement context just as the Supreme Court has done in the dealer termination context. The same criticisms that have been made above apply equally here. Formal and substantive issues should be kept separate. If substantive considerations were to be incorporated into the definition of agreement, it should only be done when free riding is a pertinent concern. And lastly, if an agreement is understood to be a meeting of the minds, common intention should suffice to establish an agreement and the substantive analysis should be undertaken subsequently. In other words, under this conception of an agreement, it is difficult to draw a distinction between a unilaterally imposed and mutually agreed RPM.

III. VARIOUS THEORIES OF AGREEMENT UNDER THE COLGATE DOCTRINE

The foregoing arguments suggest that there are no strong justifications for drawing a sharp distinction between unilaterally imposed RPM and RPM obtained through agreements and insisting on an agreement in vertical restraints. What follows is an examination of the various theories on agreement presented in the case law to determine whether there is any coherent internal logic to the concept of agreement encapsulated in the case law. It will be shown that not only does the concept of agreement lack convincing justifications in the vertical context, there is also no sound and internally consistent way to distinguish between the absence and presence of agreement.

A. *Coercion Theory*

The coercion theory is probably one of the most prominent theories presented in the pre-*Monsanto* case law on the existence of an agreement. The crux of the theory is that if the defendant does not rely on the inherent attractiveness of its product to obtain compliance with its suggested retail prices, but instead undertakes additional coercive measures to secure compliance, there is an agreement to implement the RPM and is hence illegal.[210]

The coercion theory has a long lineage. In *Bausch & Lomb*, the

209. *Id.* at 4.

210. *See* United States v. Parke, Davis & Co., 362 U.S. 29, 54 (1960) (Harlan, J., dissenting) (explaining that the majority found that the defendant impermissibly brought about compliance with prices by cutting off wholesalers who continued to sell to price-cutting retailers, and seeking assurances from retailers that they would comply with prices).

Supreme Court characterized what Beech-Nut had done in the *Beech-Nut* case as coercion through its special agents.[211] In *Simpson*, the Court again described what Parke, Davis had done in that case as coercion, asserting that "[w]e made clear in *United States v. Parke, Davis & Co.* [citation omitted] that a supplier may not use coercion on its retail outlets to achieve resale price maintenance."[212] The Court further observed that the leasing system in place in *Simpson* was coercive to the lessees because the lessees would not want to risk losing the leases.[213] In *Albrecht*, the employment of third-party agents to take the dealer's customers away and put pressure on the non-compliant dealer was also deemed to be coercive.[214] What followed in the 1970s and 1980s were a number of appellate court decisions in which the Court relied on the concept of coerced compliance with an RPM scheme, without more, to substantiate the finding of an agreement.[215] Commentators have disagreed on whether the coercion theory survived *Monsanto*. Some have argued that it did not.[216] Some have suggested that it did by referring to lower court cases since *Monsanto* that continued to use evidence of pressure or coercion as evidence that excludes the possibility of unilateral action under *Monsanto*.[217]

An important issue that needs to be examined under the coercion theory is what is the relationship between coercion and the *Colgate* right to terminate a non-compliant dealer. One would think that the greatest threat a supplier can use against a dealer is termination. There is no greater coercion to which a supplier can subject a dealer. This point is also related to the arbitrary distinction drawn by the Court between the inherent attractiveness of the product as opposed to coercive measures in *Parke*. Recall that the Court in that case asserted that a supplier cannot use coercive measures, but must rely on the inherent attractiveness of its products to induce dealers to comply with its RPM policy. The two are essentially one and the same. Coercive measures derive their effectiveness from the importance of the

211. *See* United States. v. Bausch & Lomb Optical Co., 321 U.S. 707, 722 (1944) ("The Beech-Nut Company, without agreements, was found to suppress the freedom of competition by coercion of its customers through special agents of the company, by reports of competitors about customers who violated resale prices, and by boycotts of price cutters.").

212. Simpson v. Union Oil Co. of Cal., 377 U.S. 13, 17 (1964) (citation omitted).

213. *Id.*

214. Albrecht v. Herald Co., 390 U.S. 145, 149-50 (1968), *overruled by* State Oil Co. v. Khan, 522 U.S. 3 (1997).

215. Floyd, *supra* note 18, at 292.

216. *See, e.g.*, *id.* at 298 (arguing that a literal reading of *Monsanto* says that "coerced compliance with a scheme of resale price maintenance, standing alone, is no longer a viable theory of antitrust combination or conspiracy").

217. *See, e.g.*, Harrison, *supra* note 92, at 1146 (referring to Babyage.com, Inc. v. Toys "R" Us, Inc., 558 F. Supp. 2d 575 (E.D. Pa. 2008), as evidence that coercion continued to be a relevant consideration after *Monsanto*).

supplier's business to the dealer. The supplier can do no more than to halt the supply of the product. It was noted earlier that the Supreme Court incongruently objected to the use of moderate coercion in cases such as *Beech-Nut* and *Parke* while endorsing the use of maximum coercion through termination in *Colgate*. If the *Colgate* doctrine sanctions the use of the highest level of coercion, what can the coercion theory really mean? One would assume that if coercion is to be the basis for determining when the *Colgate* right of termination has been exceeded, the benchmark would be whether a greater amount of coercion than termination has been used.

A review of the case law suggests that in *Beech-Nut* and *Parke* the so-called coercion condemned by the Court was not the use of greater coercion than termination, such as physical violence or sabotage, but the use of agents to monitor and implement compliance with a view of terminating non-compliant dealers.[218] In *Simpson*, it seems that the Court believed the coercion came from the threat of termination itself.[219] In *Albrecht*, the coercion came from the use of third-party agents to put pressure on the non-compliant dealer.[220] *Simpson*'s characterization of coercion in that case was clearly inconsistent with the *Colgate* doctrine. It effectively meant termination is coercion. The method of coercion in *Beech-Nut* and *Parke, Davis* cannot be correctly described as coercion. All that the defendant did was put in place measures to allow it to detect non-compliance and to exercise its *Colgate* right of termination.[221] The defendants did not apply any more pressure than was inherent in the right of termination.

Albrecht, however, presented an interesting case. The defendant resorted to all those measures most probably because it did not want to terminate the non-compliant dealer. This could be because the non-compliant dealer was the best dealer in the relevant geographic area and thus the defendant needed it. In other words, the defendant and the dealer had comparable bargaining power. Or perhaps the defendant thought that its threat of termination was not credible and thus the dealer did not believe that the defendant would follow through. The entire incident of employing third-

218. *See* FTC v. Beech-Nut Packing, 257 U.S. 441, 452 (1922) (holding that requiring distributors to resell products at standard prices, and refusing sale to non-compliant distributors was done in such a way to suppress competition); United States v. Parke, Davis & Co., 362 U.S. 29, 38 (1960) (ruling that enticing wholesalers to deny products to non-compliant retailers constituted price-fixing, since customers did not willingly agree to prices as a matter of individual choice).

219. *See* Simpson v. Union Oil Co. of Cal., 377 U.S. at 13, 17 (1964) (holding that threat of termination of a lease agreement unless entering into a consignment agreement was an actionable wrong).

220. *See Albrecht* 390 U.S. at 152 (demonstrating that securing compliance with resale prices by means in addition to mere policy announcement and refusal to deal would constitute an illegal combination to fix prices).

221. *Colgate*, 250 U.S. at 304.

party agents to take away the dealer's customers was to demonstrate to the dealer the consequences of termination. Whether the defendant's conduct in *Albrecht* should count as coercion would depend on whether the *Colgate* right of termination encompasses the right to demonstrate the consequences of termination. Basic logic would suggest that if A goes beyond B, the right to do A would encompass the right to do B. Moreover, if coercion was to be a coherent theory of agreement to delineate the boundary of the *Colgate* doctrine, the most sensible formulation of the theory would be that the defendant cannot exceed the amount of coercion inherent in termination. If that is the case, it is clear that the amount of coercion entailed by a demonstration of the consequences of termination can be no greater than actual termination itself. Therefore, the Supreme Court has failed to articulate persuasively the precise nature and scope of coercion that would take the defendant outside the protection of the *Colgate* doctrine. What should count as coercion under a coherent theory of coercion would be, for example, the defendant's threat to terminate multiple lines of business with the dealer following the dealer's non-compliance of minimum prices in one line of business.

Furthermore, the coercion theory is subject to the criticism articulated earlier that it is futile to inquire into the degree of coercion to which the parties are subject. Unless there is a complete alignment of interests between the supplier and the dealer in the use of RPM, there is always a degree of coercion involved. The degree of coercion also provides little useful information, such as the likelihood that the RPM scheme is being used anticompetitively or pro-competitively. What the degree of coercion involved in an RPM scheme tells us is the relative bargaining power of the parties, the extent to which the parties' interests coincide, and the credibility of the threat to terminate the relationship, none of which sheds light on the ultimate issue of the competitive effects of the RPM scheme.

Ultimately, the greatest flaw of the coercion theory is its logical inconsistency. If an agreement is understood to be a meeting of the minds, it signifies voluntary assent to a common course of action or joint enterprise. The more voluntary the assent is, the stronger the claim that the parties have agreed. Under the coercion theory, however, the more coerced a party is to accede to the counterparty's request, the more likely that there is an agreement. In other words, coerced compliance gives rise to an agreement while willing compliance does not.[222] This is obviously counter-intuitive. If anything, as was argued in *Perma Life Mufflers*, it would seem that there is less of an agreement when one party is coerced because there is less free

222. *See* Floyd, *supra* note 18, at 295 (stating that unwilling compliance should be sharply distinguished from willing compliance regarding a supplier's suggested resale prices).

will.[223] Robinson notes that "[i]t seems hardly necessary to argue that coercion of dealers is not only not the same as an agreement but also is inconsistent with the existence of an agreement taken in its ordinary sense to imply voluntary assent."[224] The reason for such a counter-intuitive theory is the conflation of the existence of an agreement with the blameworthiness or the anticompetitiveness of the conduct. While it may make sense to say that the use of coercion to achieve one's objective is objectionable and therefore may render it more problematic under antitrust law, it certainly does not make sense to say that the use of coercion creates an agreement.

The incongruity of this notion is highlighted by the seemingly direction-specific nature of this theory. In the usual application of this theory, the supplier is the source of coercion. But this need not be the case. The source of coercion could be a powerful dealer. According to the case law, when a supplier uses coercive measures to enforce an RPM scheme, there is an agreement. In contrast, when a dealer exerts pressure on the supplier to terminate a price-cutting dealer, there is not necessarily an agreement. One still needs to inquire whether the supplier terminated the non-compliant dealer on its own free initiative, or only due to pressure from the complaining dealer.[225] While this is sound as a matter of substantive analysis, there is no logical basis as a matter of the coercion theory to distinguish between coercion from a supplier and that from a dealer. Both could be equally coercive if coming from a party with a great deal of bargaining power. The only explanation for this incongruous outcome is that coercion is being used as a proxy for substantive analysis, especially coercion originating from a dealer.

B. *Enforcement Theory*

The enforcement theory of agreement can be said to overlap with the coercion theory to some extent, since the Court seemed to define coercion as adopting additional measures to monitor compliance and put pressure on dealers. The Court in *Parke, Davis* stated that the reason additional enforcement efforts are objectionable is because they coerce.[226] The theory essentially determines the existence of an agreement based on the amount of

223. *See* Robert Pitofsky & Kenneth W. Dam, *Is the Colgate Doctrine Dead?*, 37 ANTITRUST L.J. 772, 778 (1968) (explaining that *Colgate* protection is more likely to apply when parties enter into an agreement voluntarily).

224. Robinson, *supra* note 24, at 600.

225. Hovenkamp, *supra* note 24, at 6, 13 (contemplating the relationship between a termination and the cause).

226. *Parke, Davis*, 362 U.S. at 46-47 (stating that organizing a conspiracy or combination of traders to promote compliance with suggested resale prices was sufficient additional to mere termination).

effort the supplier has exerted to implement, monitor, and police the RPM scheme. The general idea is that the greater is the enforcement effort, the more likely that there is an agreement.

A number of cases provide the basis for the theory. The earliest case in which the Court can be said to have propounded the theory was *Beech-Nut*, in which the Court held that a company cannot rely on methods to secure compliance with an RPM scheme that are as effective as an express or implied agreement.[227] The Court found particularly troubling conduct such as compiling lists of non-compliant dealers to which no supply was to be made, using salesmen and agents to monitor compliance, and using numbers and symbols to help track products.[228] In *Bausch & Lomb*, the Court emphasized the defendant's reliance on its wholesalers to enforce the RPM scheme.[229] The Court also mentioned espionage, institution of a licensing scheme for retailers and exclusive reliance of licensed dealers, and the use of a protection certificate to identify non-compliant wholesalers.[230] In *Parke, Davis*, it seems that the only additional enforcement effort the defendant undertook — apart from soliciting compliance from retailers directly not to advertise discounted products, which would clearly count as an agreement — was the use of wholesalers to help police the RPM scheme. Finally, the *Albrecht* court objected to the defendant's recruitment and use of third-party agents to solicit the non-compliant dealer's customers and to serve these customers.[231]

A review of these cases suggests certain trends in the case law in what the Supreme Court finds problematic. First, the Court clearly objected to the use of third parties, be they unrelated agents or wholesalers, to solicit compliance. Second, the Court seemed to take issues with monitoring efforts, either by own employees or third-party agents, of dealer compliance or through the use of measures that allow tracking of products.[232] Third, the Court seemed to have problems with the institution of a formal punitive mechanism through the compilation of offender lists or other means.

One central issue in the enforcement theory is the delineation of permissible and impermissible enforcement efforts and measures. In his

227. FTC v. Beech-Nut Packing Co., 257 U.S. 441, 455 (1922).

228. *Id.* at 456.

229. United States v. Bausch & Lomb Optical Co., 321 U.S. 707, 723 (1944).

230. *Id.* at 721.

231. *See Albrecht*, 390 U.S. at 147 (objecting to the use of a solicitation service).

232. *See* Carl H. Fulda, *Individual Refusals to Deal: When Does Single-Firm Conduct Become Vertical Restraint?*, 30 L. & CONTEMP. PROBS. 590, 604-05 (1965) (defining unilateral refusal as acceptable when detection of price cutting is unsolicited and solely the result of the manufacturer's own effort); *see also* Pitofsky & Dam, *supra* note 223, at 779 (arguing that even techniques like open and systematic shopping done solely by the seller can still be construed as means extending beyond *Colgate* rights).

dissent in *Parke, Davis*, Justice Harlan argued that the defendant's enforcement efforts were much less elaborate in that case than in *Beech-Nut* and *Bausch & Lomb* and did not warrant condemnation.[233] In fact, commentators have argued that after *Parke, Davis*, what was within the scope of permissible conduct was unilateral announcement of policies and refusal to deal with non-compliant dealers.[234] Drawing the line of permissible enforcement measures at the very boundary of the *Colgate* doctrine itself is certainly possible. However, doing so would defeat the purpose of the theory if it was meant to delineate the boundary between concerted action and unilateral conduct beyond the *Colgate* doctrine. It is not even clear if this boundary is logically consistent. Termination of a non-compliant dealer constitutes an enforcement measure, and perhaps the most heavy-handed one at that. If the enforcement theory prohibits any enforcement effort, it should prohibit termination as well. That would effectively amount to the repudiation of the *Colgate* doctrine.[235] Under this formulation of the theory, the only permissible exercise of the *Colgate* right would be in the initial selection of dealers. Presumably the refusal to make an initial selection of a dealer constitutes more as the institution rather than enforcement of an RPM scheme. This is effectively the theory pursued by the FTC in the *Russell Stover* case.[236] The enforcement theory also seems to contradict the essence of the *Colgate* doctrine. If the doctrine stands for the proposition that at least some RPM schemes are permissible, then it is not clear why efforts to enforce them should render these schemes illegal. This is tantamount to giving someone a legal right but prohibiting him from enforcing it. Allowing a firm to adopt RPM must entail giving it the power to adopt reasonable measures to implement it.

Assuming that Justice Harlan was correct and *Parke, Davis* had in fact gone too far, then it is worth trying to delineate the scope of permissible enforcement. The case law is quite clear that the use of agents is impermissible. While one may concede that the use of agents to inflict

233. *See Parke, Davis*, 362 U.S. at 55-56 (explaining that unilateral behavior otherwise permissible should not be deemed impermissible due to similar unilateral action at the retail level). *But see Beech-Nut*, 257 U.S. at 455 (holding that an organized, effective enforcement effort constituted unfair methods of competition); *see also Bausch & Lomb*, 321 U.S. at 723 (inferring from the aggressive, widespread, highly organized programs that this was impermissible conduct).

234. *See* Kathryn A. Kusske, *Refusal to Deal as a Per Se Violation of the Sherman Act: Russell Stover Attacks the Colgate Doctrine*, 33 AM. U. L. REV. 463, 471-72 (1984) (arguing that after *Parke, Davis*, the *Colgate* doctrine only protected two manufacturer actions: the right to announce policy, and the right to refuse to deal with noncompliant retailers).

235. *See Colgate*, 250 U.S. at 304 (1919) (holding that a company may unilaterally withhold or terminate business without violating antitrust law).

236. *See* Russell Stover Candies, Inc. v. FTC, 718 F.2d 256 (1983) (holding that a candy manufacturer's mere refusal to sell at certain prices did not constitute unlawful coercion).

punishment on a non-compliant dealer crosses the line, it is much harder to defend the condemnation of the use of wholesalers. The reliance on wholesalers to police and give effect to an RPM scheme may merely reflect the fact that the supplier does not deal with the retailers directly and must go through wholesalers to sell to retailers. In that case, there is no way a supplier can terminate a non-compliant dealer without making use of the wholesaler. There is simply no direct relationship between the supplier and the retailer to terminate. The only way supply to the offending retailer can be terminated is by instructing the wholesaler to stop selling to the retailer. There is no way for such a supplier to exercise its *Colgate* right without going through its wholesalers. As argued earlier, if the Court were to outlaw the use of wholesalers in the implementation of an RPM scheme, the Court would be effectively offering preferential treatment to firms that deal directly with their retailers. This may be merely a function of the industry structure or the nature of the product. A rule that allows firms dealing directly with their retailers but not those dealing with retailers through wholesalers to impose RPM is arbitrary at best and lacks any sound economic justification.

The Court's prohibition of monitoring effort and adoption of punitive mechanisms such as an offender's list is equally perplexing. If the *Colgate* doctrine allows a supplier to terminate a non-compliant dealer, it must by implication allow the supplier to make effort or put in place a system to detect non-compliance. Otherwise, the *Colgate* right of termination would ring hollow. Therefore, the use of employees or third parties to monitor compliance and the institution of a system to track products cannot be a basis for finding an illegal agreement. This is especially true after *Monsanto*, which clearly sanctioned the use of dealers to monitor compliance of other dealers.[237] There is no logical reason to allow the use of dealers on the one hand and to prohibit the use of employees and other third parties on the other hand. It is also unclear what is objectionable about compiling a list of offenders which may be subject to termination. Such a list may serve two functions. One is to let wholesalers know which retailers they are to stop selling to. If the use of wholesalers to implement an RPM scheme is allowed, the supplier must be permitted the means to communicate with its wholesalers concerning implementation, such as to whom the wholesalers can sell. Another function is to warn offending dealers about possible termination. If a supplier is allowed to terminate a non-compliant dealer, surely it must be allowed to give advanced warning to such a dealer prior to termination. In short, none of the bases upon which the Court attempted to distinguish between permissible and impermissible enforcement are tenable. If the enforcement theory were to form the basis for delineating the boundary

237. Correia, *supra* note 53, at 202.

of permissible unilateral conduct, there must be a logically consistent and defensible principle for distinguishing permissible from impermissible enforcement.

C. *Effectiveness Equivalence Theory*

The effective equivalence theory has not been as widely propounded as the coercion theory and the enforcement theory. Its genesis lies in the *Beech-Nut* case, in which the Supreme Court proclaimed that "[t]he specific facts found show suppression of the freedom of competition by methods in which the company secures the co-operation of its distributors and customers, which are quite as effectual as agreements express or implied intended to accomplish the same purpose."[238] Levi notes that this proclamation from the Court introduced significant uncertainty to the *Colgate* doctrine.[239] The notion that methods of implementation that are as effective as an express or implied agreement will be condemned was reaffirmed in *Parke, Davis*, in which the Court made reference to the holding in *Beech-Nut* that firms cannot use methods of implementation that were as effective as agreements to obtain compliance with an RPM scheme.[240]

There are a number of problems with the theory. First, the theory assumes that express and implied agreements only have one level of effectiveness, which is obviously not true. Without clearly identifying the kind of agreement that would be the comparator for the application of the theory, the theory provides little practical guidance on what constitutes permissible unilateral conduct. Second, the effectiveness of an agreement obviously depends on its enforcement mechanisms. An agreement under which the defendant is allowed to employ a full range of enforcement mechanisms will surely be more effective than if the defendant is confined to suing for breach of contract. Therefore, the effectiveness equivalence theory is necessarily tied to the enforcement theory and cannot be meaningfully applied without resolving the fundamental question under the enforcement theory. And once one has resolved the question of permissible enforcement mechanisms, it is questionable how much the effectiveness equivalence theory adds to the analysis. More fundamentally, the effectiveness equivalence is at odds with the *Colgate* doctrine. The basic premise of the *Colgate* doctrine is that methods of implementing an RPM

238. *Beech-Nut*, 257 U.S. at 455.

239. Levi, *supra* note 9, at 321.

240. *Parke, Davis*, 362 U.S. at 42 (1960); *see also* Levi, *supra* note 9, at 278 ("Mr. Justice Brennan's opinion for the Court in *Parke, Davis* sketched the growth of the relevant segment of resale price doctrine through three stages. . . [including] the proposition that illegality may be caused by any methods as effectual as agreements.").

scheme which may have the same effectiveness could result in different legal consequences. An RPM scheme implemented by an implied agreement may be no more effective than one publicized by a unilateral policy announcement and enforced by threat of termination, but the former is illegal while the latter is not. Therefore, the effectiveness equivalence theory cannot be applied to determine the boundary of the *Colgate* doctrine.

D. *Economic Interest Theory*

The economic interest theory can be attributed to Justice Harlan's dissent in *Albrecht*, in which he argued that it was erroneous for the majority to infer an agreement between the newspaper publisher and the agents because the latter had no economic interest in the success of the defendant's vertical price ceiling scheme.[241] Justice Harlan further rejected the claim that there could be an agreement among the different dealers of the publisher because the dealers did not share any common economic interest. Whether one dealer complies with the price ceiling scheme mattered little to other dealers.[242] He noted that "the effectiveness of a price ceiling imposed on one distributor does not depend upon the imposition of ceilings on other distributors, be they competitive or not."[243] He concluded by stating that "[f]or the manufacturer who purports to act unilaterally in dictating a maximum price really is acting unilaterally. No one is economically interested in the price squeeze but himself."[244] *Perma Life Mufflers* also endorsed the economic interest theory.[245]

There are difficulties with Justice Harlan's argument. As argued earlier, it is clear that the third-party agent had an economic interest in the agreement, the agreement being the one in which the publisher paid the agent to undertake work to undermine the non-compliant dealer. In fact, there was no question that there was an agreement between the publisher and the agent. While it is true that the agent had no interest in the success of the vertical maximum price fixing scheme, the disconnect results from the fact that the majority used an ancillary agreement as a substitute for what should be the agreement at issue, the price fixing scheme. Justice Harlan's argument was an indirect criticism of the majority's cavalier choice of agreement to focus on. But it was plainly incorrect to say that there was no agreement between the publisher and the agent.

The presence of congruent economic interests is a necessary but not a

241. *Albrecht* 390 U.S. at 161.
242. *Id.*
243. *Id.*
244. *Id.* at 163.
245. *Perma Life Mufflers*, 392 U.S. at 138.

sufficient condition for the finding of an agreement. The fact that the parties' economic interests converge does not mean that they necessarily have an agreement. Meanwhile, the converse is probably true. The absence of congruent economic interests may negate the existence of an agreement. Therefore, the most that the economic interest theory can do is to serve as a screen for plausible agreements. If the parties do not share economic interests in a common outcome, there is probably no agreement between them. The theory, however, does not provide a basis for positive identification of an agreement.

It is important to caution against a deep inquiry into the economic interests of the parties. Economic interests inform motives. When we ask whether the parties share common economic interests, we are effectively asking whether they have the motive to enter into an agreement. It was argued earlier that inquiring about motives at the stage of determining the existence of an agreement amounts to a premature consideration of substantive issues. In many instances, motives are used as a proxy for competitive effects. When it is now possible to weigh the anticompetitive effects and pro-competitive benefits openly under the rule of reason analysis, there are scant justifications for persisting with the outdated practice.

E. *Implied Acceptance Theory*

The implied acceptance theory has an illustrious academic pedigree. As early as the 1960s, Professor Turner asserts that:

> [i]f a manufacturer induces acquiescence by his distributors in a policy of resale price maintenance, he has created a series of tacit vertical agreements, and it seems wholly irrelevant to that conclusion that he obtained these tacit agreements by threats of refusal to deal, carried out against those who refused to acquiesce.[246]

The rationale is that the practical effects of the conduct are the same regardless of whether compliance was secured by an agreement or refusal to deal.[247] Professor Hovenkamp reiterates Turner's sentiment when he argues that, on the theory of an implied acceptance of the supplier's terms, "a vertical agreement can be found when there is an announced condition or its equivalent on future dealing, the sanction for noncompliance is credible, and the market effects are proved or presumed to be similar to those of express

246. Donald F. Turner, *The Definition of Agreement under the Sherman Act: Conscious Parallelism and Refusals to Deal*, 75 HARV. L. REV. 655, 689 (1962).

247. *See id.* at 688 (stating that practically there is no difference between compliance secured by an agreement or refusal to deal).

agreements."[248]

The Supreme Court can be said to have implicitly endorsed the theory on at least two occasions, *Bausch & Lomb* and *Parke, Davis*. In *Bausch & Lomb*, the Court noted that the wholesalers:

> [A]ccepted Soft-Lite's proffer of a plan of distribution by cooperating in prices, limitation of sales to, and approval of retail licensees. That is sufficient. . . . Whether this conspiracy and combination was achieved by agreement or by acquiescence of the wholesalers coupled with assistance in effectuating its purpose is immaterial.[249]

In *Parke, Davis*, the Court similarly found an agreement when the wholesalers acquiesced to help implement the RPM scheme by refusal to deal.[250]

Professor Hovenkamp posits that the defendant may attempt to dispel the notion of an agreement by making very clear that "it makes no offer, requests no acceptance, and desires no dealer commitment with respect to the goods on hand" or arguing that the unilateral policy announcement only serves to provide "fair notice to dealers who might otherwise claim unfair surprise when terminated. . ."[251] If the implied acceptance theory is to have any meaningful application, it cannot be circumvented simply by resorting to semantic arguments. How the defendant characterizes its action — non-solicitation of offer or fair notice — does not change the nature of its action, which is indirectly to seek compliance with its conditions.

While the implied acceptance theory comports with common sense, there is a very fine line between the application of the implied acceptance theory and a repudiation of the *Colgate* doctrine.[252] The Supreme Court itself acknowledged that what is permitted under *Colgate* results in the same economic effects as an illegal agreement.[253] Hovenkamp himself

248. Hovenkamp, *supra* note 24 at 7.

249. Bausch & Lomb, 321 U.S. 707, 723 (1944).

250. *See Parke, Davis*, 362 at 45 (finding that the wholesaler's refusal to deal to retailers who did not adhere to *Parke Davis*' suggested retail price was a violation of the Sherman Act because of an implied agreement between *Parke, Davis* and the wholesalers).

251. Hovenkamp, *supra* note 24, at 7.

252. *See* Burns, *supra* note 61 at 19 ("Certainly, an implicit agreement in some sense was present in the Colgate situation insofar as the manufacturer made his wishes known and the conforming retailers went along because they knew that they had to comply in order to continue receiving goods."); *see also Fulda*, *supra* note 232 at 595 ("The notion that any retailer who accepts goods for distribution with knowledge of the manufacturer's announcement as to observance of retail prices gives an implied promise to comply may be logical, but, as a general proposition, it is irreconcilable with Colgate, which allows advance announcements of the circumstances under which the manufacturer would refuse to deal.").

253. *See Parke, Davis* 362 U.S. at 44 (offering a distinction between permissible and non-permissible agreements under Colgate even though they have the same economic effect).

acknowledges this, and concedes that to reconcile the theory with the *Colgate* doctrine, one must interpret the doctrine as not granting an absolute right of refusal to deal. His suggestion is to reformulate the *Colgate* doctrine as only permitting simple enforcement of the announced condition, which essentially amounts to refusal to deal, and precluding complex enforcement, which covers the range of enforcement measures prohibited by the cases from *Beech-Nut* to *Parke*.[254]

There are a number of difficulties with this reformulation. First, if the benchmark for equivalence is practical or market effects, there is no reason to accord different treatment to simple enforcement and complex enforcement. The fact of the matter is that regardless of the enforcement mechanism, degree of coercion, or other details of implementation of an RPM scheme, if the scheme achieves its intended result, it produces the same market effects. Therefore, drawing a distinction between simple and complex enforcement is inconsistent with the very basis of the theory. Second, if the theory is formulated to accommodate only simple enforcement, it amounts to a restatement of the *Colgate* doctrine and adds nothing to it. In that case, the theory performs no useful function. Lastly, under the suggested reformulation, the theory effectively morphs into the enforcement theory with all its attendant problems. If the determinant of legality is to be the amount of enforcement, one would be better off adopting the enforcement theory and focus on the relevant issues head-on.

Another possible reformulation of the theory to accommodate the *Colgate* doctrine is to focus on the amount or nature of individualized dealing between the supplier and the dealer. Such conduct may include targeted announcement of the condition of compliance to a non-compliant dealer, warning of detection of non-compliance, perhaps in the form of a circulation of the offenders' list as in *Beech-Nut*, or even reinstatement of a terminated dealer after reassurance by the dealer of future compliance. It is certainly plausible to argue that when such individualized communication has taken place, the parties have reached an agreement. When a targeted announcement or an individual warning is made, a strong argument can be made that the supplier is actively soliciting compliance from a specific dealer. Reinstatement of a dealer in exchange for reassurance of compliance encapsulates an agreement.[255] However, if that is where the implied

254. *See Hovenkamp*, *supra* note 24 at 8 (suggesting that there is a distinction between simple and complex refusals to deal).

255. *See* Warren S. Grimes, *The Path Forward After Leegin*: *Seeking Consensus Reform of the Antitrust Law of Vertical Restraints*, 75 ANTITRUST L.J. 467, 489-90 (2008) ("The termination of a discounting dealer and, after a relatively short period, its reinstatement might constitute a non-verbal understanding or agreement on resale pricing that nullifies the defense."); *see also* Fulda, *supra* note 232 at 596 ("Manufacturers should consequently be cautious in offering conditions under which dealings previously terminated would be

acceptance theory draws the line between permissible unilateral conduct and illegal concerted action, it does not add much to the conventional understanding of an agreement. One need not resort to the theory to conclude that such individualized communication amounts to an agreement. The kind of communication at issue verges very close to direct, explicit communication, which has always been a basis for agreement.

F. *Communication Theory*

The communication theory can be said to originate from footnote 9 in *Monsanto*, in which the Supreme Court asserted that:

> [t]he concept of 'a meeting of the minds' or 'a common scheme' in a distributor-termination case includes more than a showing that the distributor conformed to the suggested price. It means as well that evidence must be presented both that the distributor communicated its acquiescence or agreement, and that this was sought by the manufacturer.[256]

In essence, this footnote requires communication in which the manufacturer seeks compliance and communication in which the dealer offers compliance. There is some ambiguity as to the nature of communication required. Hay argues that this requirement is tantamount to mandating a formal offer and acceptance and that implied acceptance no longer suffices.[257] In fact, after *Business Electronics*, it is not even enough to show that there was an express discussion between the supplier and the dealers about prices. It must be shown that there was an agreement about price or price level. This was affirmed in the Fifth Circuit *Leegin* case after remand from the Supreme Court. In rejecting the plaintiff's argument that there was an agreement between Leegin and its dealers on price in light of evidence of discussion of special occasion discounts between them in Hawaii, the Fifth Circuit held that "[a] manufacturer's discussion of pricing policy with retailers and its subsequent decision to adjust pricing to enhance its competitive position do not create an antitrust violation or give rise to an antitrust claim."[258]

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resumed, lest such negotiations, if successful, be interpreted as contracts rather than unilateral announcements."); Pitofsky & Dam, *supra* note 223 at 779 ("The distributor who fails to abide by the seller's conditions cannot be restored — at least not for a substantial period of time — because acceptance by the distributor of his old status rightly will be viewed as an assurance of compliance.").

256. Monsanto Co. v. Spray-Rite Serv. Corp., 465 U.S. 752, 764, (1984).

257. *See* Hay, *supra* note 10, at 435 (suggesting "that something close to a formal offer and acceptance is necessary, and that the distributor's mere adherence to the suggested price is not an adequate acceptance").

258. PSKS, Inc. v. Leegin Creative Leather Prods., Inc., 615 F.3d 412, 420 (5th Cir.

The communication theory imposes a very high threshold for establishing an agreement. If the commentators and the lower courts have interpreted *Monsanto* and *Business Electronics* correctly, it essentially requires nothing short of an express agreement that stipulates the resale price level. This is nothing short of a sea change in the law on vertical agreement. This approach is commendable in the sense that it provides a very clear standard for determining the existence of an agreement. It is arguably a mirror image of the *Colgate* doctrine, which can be read to suggest that anything more than unilateral policy announcement together with enforcement by a refusal to deal amounts to an illegal agreement. Under the communication theory as propounded in *Monsanto*, anything short of an express agreement on price is permissible unilateral conduct. However, such a theory suffers from many drawbacks. It is economically unsound, and is inconsistent with prior case law on vertical agreements and horizontal agreements. First, as noted by Hay, there is no reason to distinguish between an RPM scheme achieved by an express agreement and other methods from an economic perspective because their economic effects are the same.[259] While this argument can be applied to any attempt at line drawing between unilaterally imposed RPM and an illegal RPM agreement, it carries particular weight in this instance because an insistence on a formal agreement on price elevates form over substance, which has long been frowned upon by the antitrust law. One cannot place a greater premium on formality than what is allegedly required under the communication theory.

This insistence on formality in the vertical context has been repudiated by the Supreme Court since *Schrader's Son*, when the Court declared that an agreement in the vertical context can be expressed or implied.[260] This assertion has been repeatedly given express or implicit affirmation by the Court ever since. Floyd argues that *Monsanto* has implicitly overruled these decisions. He further argues that the communication theory is much less defensible than other attempts to articulate a theory on vertical agreements.[261] There are strong arguments that the Court should not be deemed to have

2010).

259. *See* Hay, *supra* note 10, at 435 (stating "the economic effect of the distributors' compliance is identical to that of a formal agreement").

260. *See* United States v A. Schrader's Son Inc., 252 U.S. 85, 99 (1920) (distinguishing between a company that indicates its wishes regarding prices and formal agreements, express or implied).

261. *See* Floyd, *supra* note 18, at 300 ("In terms of the policies underlying antitrust conspiracy doctrine, the line that the Commission attempted to draw in Russell Stover between coerced acquiescence and willing compliance with suggested resale prices is much more defensible than the Supreme Court's dictum in Monsanto, which rests the question of illegality on whether the supplier sought and obtained a 'communication' of acquiescence or agreement.").

repudiated decades of case law and such a strongly established rule without detailed examination of the case law and an explicit overrule.

There are a number of ways to reconcile the language in *Monsanto* with the decades of case law on vertical agreement. First is the acknowledgement that the *Monsanto* court did not go as far as Hay argues and did not actually *require* express communication. Implied or indirect communication would still suffice and footnote 9 in *Monsanto* was not meant to change the decades of case law on how an agreement can be proved, at least in so far as the supplier's and the dealer's conduct can be construed as communication.[262] Second, as previously argued, a more careful reading of *Monsanto* and *Business Electronics* suggests that the holding of those two cases were meant to be limited to dealer termination cases. They were not meant to disturb the ways in which an agreement can be proved in cases absent dealer termination. As Hay observes, "[T]he Monsanto Court seems to confer an elevated independent status for the manufacturer's right to refuse to deal."[263] The merit of such an elevation notwithstanding, it at least amounts to recognition that dealer termination cases are meant to be treated differently from other RPM cases. Lastly, and most importantly, whatever strict approaches the Court adopted in *Monsanto* and *Business Electronics* were clearly motivated by the *per se* rule prevailing when those cases were decided. Once the *per se* rule has been overruled, there are no good justifications for treating RPM cases and dealer termination with such circumspection and for adopting such a cautious approach to the proof of an RPM agreement. Once all these arguments are accepted and it is conceded that implicit communication may give rise to an agreement, the communication theory amounts to nothing more than our conventional understanding of agreement applicable to both horizontal and vertical restraints.

In conclusion, none of the theories on agreement put forward by the case law are logically coherent or theoretically sound nor do they provide meaningful guidance on how to distinguish between permissible unilateral conduct and illegal concerted action. The attempt to draw a line between these two concepts under the *Colgate* doctrine remains beset with ambiguity. Perhaps the only logically defensible line one can draw is at the doctrine itself, under which the defendant is allowed to unilaterally announce its policy and terminate non-compliant dealers without any further engagement or communication, and nothing more.

262. However, this may open to question the continual validity of the enforcement theory and the effectiveness theory, under which it is hard to characterize triggers for the application of the theories as communication.

263. Hay, *supra* note 10, at 435.

IV. ECONOMIC JUSTIFICATIONS FOR AN AGREEMENT REQUIREMENT

Having established that there is no logically coherent and theoretically sound basis for drawing the boundary between permissible unilateral conduct and illegal concerted action under the *Colgate* doctrine, it remains to be determined whether there is any economic basis for the doctrine. A number of commentators such as Hay and Justice Brennan in *Parke, Davis* have acknowledged that focusing on the economic effects of the conduct, there is no clear distinction between the conduct permitted by the doctrine and that which is prohibited.[264] A closer examination of the various economic theories and models confirms the observation that the notion of agreement serves no important function as far as the analysis of economic effects is concerned.[265]

A. *Economic Theories of Harm for RPM*

A variety of theories of harm have been proposed for RPM in the economic literature. In general, the theories can be categorized under two headings: those involving cartels or coordinated action, either at the supplier or the dealer level, and those involving a powerful supplier or dealer exercising market power. In the first category, the two most prominent theories of harm are the facilitation of a supplier cartel and the facilitation of a dealer cartel. However, RPM does not only harm competition when a cartel is involved. It can harm competition between firms at the supplier level when multiple firms employ RPM, even in the absence of a cartel.[266] In the second category, RPM may harm competition when a powerful dealer uses it to foreclose innovation in distribution and when a powerful supplier uses it to foreclose rival access to effective distribution channels.[267] Even in the absence of foreclosure, RPM employed by a single firm can still harm the welfare of inframarginal consumers when certain conditions are met.

264. *Parke, Davis*, 362 U.S. at 512 (conceding that the economic effects of unlawful concerted actions under Colgate are the same as lawful individual conduct).

265. *See* Robinson, *supra* note 24, at 592 (arguing that Jean Burns "perceptively" shows that there is no connection between the vertical agreement and the anticompetitive effects of resale price maintenance).

266. *See* Robert L. Steiner, *How Manufacturers Deal With the Price-Cutting Retailer: When are Vertical Restraints Efficient?*, 65 ANTITRUST L.J. 407, 407 (1997) (arguing that it frequently benefits the manufacturer to adopt restraints voluntarily, in the absence of cartels, and that these actions can adversely affect competition by creating barriers to entry of new, more efficient retailers).

267. *See id.* (explaining that what might be privately efficient for a manufacturer might retard the entry of more efficient retailers).

1. Facilitation of Supplier Cartel

Telser first articulated the possibility that RPM can be used to facilitate a supplier or manufacturer cartel.[268] More recently, Jullien and Rey explain the function played by RPM in a supplier cartel as follows:

> The basic idea is that, because manufacturers can more readily observe rivals' retail prices than rivals' wholesale prices, RPM helps manufacturers to detect deviations from a collusive agreement. Whenever manufacturers cannot perfectly infer wholesale prices from retail prices, they may find it more effective to collude directly on retail prices through RPM. . . . Under RPM, retail prices are centrally set by the manufacturer and thus do not fully adjust to these local shocks on the retail environment. As a result, retail prices are more uniform under RPM and deviations from an agreement are thus easier to detect, which facilitates collusion.[269]

RPM also reduces the incentive to cheat in a supplier cartel. Secret discounts to retailers become less profitable as the retailers cannot pass on the discounts to increase sales.[270] Offering secret discounts to retailers will only lower the supplier's revenue.

According to Jullien and Rey, fixed resale prices are not without costs. The price rigidity resulting from RPM would prevent prices from adjusting to local shocks.[271] Moreover, RPM may render collusion more fragile as defections may become more attractive as flexible prices allow the suppliers to take advantage of the retailers' local information.[272] Therefore, when deciding whether to employ RPM to facilitate the detection of collusion, the supplier faces a trade-off. Flexible prices generate higher profit and stabilize collusion but make it more difficult to detect defections.[273] Fixed prices remove price fluctuations resulting from local cost changes or demand shocks, thereby stabilizing the supplier cartel.[274] RPM would not be

268. Lester G. Telser, *Why Should Manufacturers Want Fair Trade?*, 3 J.L. & ECON. 86, 96-99 (1960).

269. Bruno Jullien & Patrick Rey, *Resale Price Maintenance and Collusion*, 38 RAND J. ECON. 983, 985 (2007).

270. *See* Kenneth G. Elzinga & David E. Mills, *Leegin and Procompetitive Resale Price Maintenance*, 55 ANTITRUST BULL. 349, 359 (2010) (Elzinga & Mills I) ("If manufacturers who engage in price fixing enforce RPM agreements with their retailers, the profitability of offering secret discounts to those retailers is reduced.").

271. *See* Jullien & Rey, *supra* note 269, at 985.

272. *Id.*

273. *See id.* (arguing that flexible retail prices generate higher profits but make it more difficult to detect deviations from tacit collusion).

274. *See* Frank Mathewson & Ralph Winter, *The Law and Economics of Resale Price Maintenance*, 13 REV. IND. ORG. 57, 65 (1998) (arguing that RPM can enhance cartel stability

worthwhile if the monopoly price level was sustainable without RPM.[275] It also would be difficult to sustain if local shocks were very important.[276]

Facilitation of supplier cartels is obviously harmful from a competition perspective. Jullien and Rey show in their model that RPM is likely to be detrimental to consumer welfare as average prices will increase substantially.[277] RPM is particularly harmful when local shocks are mostly cost shocks and not demand shocks.[278] In that case, RPM results in retail prices that are both higher on average and unresponsive to local cost fluctuations.[279] Nothing in Jullien and Rey's analysis requires a formal agreement. All the effects they predict can result from the kind of unilateral conduct sanctioned by *Colgate*.[280]

2. Facilitation of Dealer Cartel

RPM can be used to facilitate dealer cartels, whereby the dealers effectively use the supplier as an enforcer of the cartel.[281] Termination by the supplier will become the punitive mechanism for policing the cartel, which is probably one of the most effective enforcement mechanisms. The dealers agree on a retail price among themselves and ask the supplier to impose the agreed price as the minimum resale price upon the dealers.[282]

Correia describes a number of different scenarios for dealer cartels. The first is an interbrand cartel, under which the colluding retailers require all

by eliminating retail price variation).

275. This may be possible already with two-part tariffs. *See* Jullien & Rey, *supra* note 269, at 992 (showing that RPM cannot be profitable when prices close to the monopoly level are already sustainable with two-part tariffs).

276. *See id.* (demonstrating that RPM is unlikely to be profitable when local shocks are too important because the cost of price rigidity would offset any increase in collusive prices).

277. *See id.* at 985 (arguing that RPM is likely to be undesirable because manufacturers will adopt it when doing so increases prices to a point that reduces consumer welfare).

278. Jullien and Rey asserted that "[i]t is well known that consumers and society as a whole prefer retail prices that adjust to cost shocks but not to demand shocks." *Id.* at 995.

279. *See id.* (concluding that RPM results in prices that are both higher on average and nonresponsive to cost conditions).

280. Even though in their model, Jullien and Rey describe the manufacturer as offering a contract, it is clear that what this contractual offer entails is merely a declaration of the terms on which the manufacturer will deal with the dealers. There is no need for negotiation or express or implied communication of acceptance. All that matters is that the dealers adhere to the announced conditions. *See id.* at 986-87 (setting forth a model of agreement that simplifies negotiations and formal agreement processes).

281. *See* Elzinga & Mills I, *supra* note 270, at 359 (stating that "retailers enlist manufacturers as a cartel's enforcer and use the manufacturer's RPM policy as a cover for the cartel's own price-fixing conspiracy").

282. *See* Calvani & Berg, *supra* note 9, at 1184 (explaining that resale price maintenance serves as a monitoring mechanism to police recalcitrant cartel members).

brand manufacturers to impose an RPM.[283] The effect of such a cartel would be no different from a supplier cartel.[284] Correia, however, argues that such a cartel is difficult to organize and maintain.[285] The second is the conventional intrabrand cartel, under which only the prices for one supplier are fixed.[286] The impact of such a cartel is less pernicious because consumers are still afforded other options, which should constrain the extent of price increase that the dealers can demand. The third is parallel conduct by multiple dealers.[287] A number of dealers may make the same demand on the supplier to raise resale prices. Correia argues that such a situation presents great difficulty for antitrust enforcement as it could be the result of a cartel or completely legitimate requests from dealers to secure a normal return for their investments in sales and after-sales services.[288] Such parallel requests need not be anticompetitive.

The obvious question to ask is why a supplier would agree to facilitate a dealer cartel. A supplier has nothing to gain from acquiescing to it.[289] Many commentators agree that for this theory of harm to be plausible, there must be an adequate account of the supplier's incentive.[290] For the dealers to be able to cajole the supplier into cooperating, they must collectively wield market power. Baxter posits that this theory of harm would only apply if there were very few distributors and substantial difficulties which prevented the suppliers from introducing additional distribution outlets.[291] Mathewson and Winter argue that one of the conditions for the dealer cartel theory is that

283. *See* Correia, *supra* note 53, at 224 (describing interbrand cartels as arising when "the cartel pressures all the suppliers in a market to institute minimum dealer prices").

284. *See id.* (highlighting the similarities between interbrand cartels and supplier cartels).

285. *See id.* at 225 (characterizing an interbrand dealer cartel as hard to organize and enforce).

286. *See id.* ("Dealers from one supplier can, in theory, can pressure the supplier to impose RPM on all the dealers.").

287. *See id.* at 227.

288. *See id.* at 228 ("When high price dealers demand that their suppliers terminate discounters, they may not be attempting to force retail prices over competitive levels in order to earn excess profits. They may simply be complaining that they cannot earn normal profits at the price charged by discount dealers.").

289. Calvani & Berg, *supra* note 9, at 1184 (stating that a resale price maintenance policy usually does nothing to support the manufacturer's interests).

290. *See, e.g.*, Marvel & McCafferty, *supra* note 179 at 347 (1984) (stating "A second requirement of an acceptable theory is that it establish some direct benefit to the manufacturer sufficient to warrant participation. While manufacturers sometimes capitulated to dealers' pressure, such pressure is inadequate to explain manufacturers' apparent fondness for RPM.").

291. *See* William F. Baxter, *Vertical Restraints and Resale Price Maintenance: A 'Rule of Reason' Approach*, 14 ANTITRUST L. & ECON. REV. 13, 24 (1982). (positing that if the number of potential distributors were very few and there were substantial difficulties preventing manufacturers from creating additional distribution outlets, distributors might employ RPM).

dealers have made substantial investments in traditional, low-volume outlets, which are threatened by the entry of discount outlets.[292] The traditional retailers would then use a supplier-facilitated cartel to block the entry of the discounters to protect their quasi-rent.[293] The dealer cartel theory is not without criticisms. A number of commentators have noted that the theory is implausible given the conditions that are required for the theory to hold true.[294]

Again, the use of RPM to facilitate a dealer cartel does not necessitate an agreement, especially after *Monsanto* and *Business Electronics*, which gave substantial leeway for dealer complaints about price-cutting dealers and legitimate communication between supplier and dealers even concerning prices.[295] The kind of communication necessary for the dealers to have with the supplier to demand a supplier-facilitated cartel can be easily disguised as a dealer complaint. In fact, if the Fifth Circuit *Leegin* case is an accurate indication of how courts will treat supplier-dealer communications in the future, dealers may not even need to disguise their request as a price complaint. After the initial demand for a cartel has been conveyed, it can be arranged through the kind of unilateral conduct permitted under *Colgate*.[296] In short, the use of an RPM scheme to facilitate a dealer cartel can be achieved without an agreement.

3. Cumulative Effects of Multiple RPM Schemes Absent Cartel

Rey and Vergé show that even in the absence of an outright cartel, RPM can be used by multiple suppliers to coordinate their prices at the monopoly level.[297] For the model to apply, there must be an interlocking relationship between the suppliers — they must sell through the same multi-brand

292. *See* Mathewson & Winter, *supra* note 274, at 65 (using retail drug stores in the US and grocery outlets in Europe during the entry of large discounts as examples).

293. *See id.* (describing the effect of this "cartelization" as the delaying or blocking of discount stores' entry).

294. *See, e.g.*, Kenneth G. Elzinga & David E. Mills, *The Economics of Resale Price Maintenance*, in 3 ISSUES IN COMPETITION LAW AND POLICY 1841, 1846 (2008) (Elzinga & Mills II); Marvel & McCafferty, *supra* note 179, at 365.

295. *See Monsanto*, 465 U.S. at 764 (holding that standard for determining violation depended on direct or circumstantial evidence of a conscious commitment to a common scheme designed to achieve an unlawful objective by the manufacturer and others); *see also Business Electronics*, 485 U.S. at (1988) (deciding that vertical restraints are not per se illegal without including some agreement on price or price levels).

296. *See* Robinson, *supra* note 24, at 598 (explaining that a successful use of vertical restraints to affect a cartel depends on the supplier's market power and monitoring ability, neither of which hinge on an agreement).

297. Patrick Rey & Thibaud Vergé, *Resale Price Maintenance and Interlocking Relationships*, 58 J. IND. ECON. 928 (2010).

retailers — and the suppliers must be able to charge a two-part tariff, consisting of both a per-unit wholesale price for the product and a flat fee.[298] Monopoly prices will be achieved regardless of whether the retailers have market power. The amount of retailer market power will only determine how the monopoly rent is split between the suppliers and the retailers.[299] The function of the two-part tariff is to allow the suppliers to share in the monopoly profit — or even to expropriate the entire monopoly profit.[300] The flat fee that the suppliers levy on the retailers is based on the overall revenue of the retailers, which includes sales of products of all brands. This profit-sharing mechanism causes the manufacturers to take into account the impact of their pricing decisions on other manufacturers, and prices to converge to the monopoly level.[301] However, monopoly prices can only be attained in the absence of intrabrand competition among retailers. Once retailers engage in intrabrand competition, retail prices will drop below the monopoly level and the manufacturers will raise wholesale prices so that they capture more of the overall profit through wholesale margin, rather than flat-fee profit sharing.[302] According to Rey and Vergé, without RPM,

> [t]he existence of competition at both the upstream and downstream levels maintains retail prices below the monopoly level. This is because, as noted above, manufacturers only take into account the retail margin on rival products, and thus fail to account that a reduction in their own prices hurts their rival's upstream profits. . . . The situation is then formally the same as if the two manufacturers were directly competing against each other.[303]

This is where RPM comes in. RPM eliminates intrabrand competition, which helps to maintain retail prices at the monopoly level, which in turn gives the manufacturers the incentive to keep wholesale prices at cost. At-cost wholesale prices minimize interbrand competition, as the manufacturers effectively pool their profits through the retailers and share them through the flat fees.[304] In other words, interbrand competition is eliminated by the virtue of the interlocking relationships and the two-part tariff mechanism. Intrabrand competition is eliminated by the RPM, which helps to sustain monopoly prices. In the presence of RPM, it is always possible for wholesale

298. *Id.* at 930, 943.
299. *See id.* at 945 ("In a double common agency situation, manufacturers must now ensure that retailers get at least as much as they could obtain by selling exclusively the rival brand; as we will see, this implies that manufacturers must leave a rent to retailers – that is, they cannot extract all the industry profits, even if they can make take-it-or-leave-it offers.").
300. *Id.* at 943.
301. *Id.* at 930, 935.
302. *Id.* at 930, 938.
303. *Id.* at 936.
304. *Id.* at 930, 937.

prices to be at cost and for retail prices to be at the monopoly level.[305] Their model illustrates that upstream and downstream competition is interrelated. The lack of downstream intrabrand competition could curtail upstream interbrand competition.[306] Rey and Vergé point out that these anticompetitive effects cannot be produced by other vertical restraints.[307] Even though RPM essentially creates an industry-wide cartel, there is no need for any industry-wide negotiation.[308] In fact, all that is required is the setting of minimum resale prices that can be accomplished under the *Colgate* doctrine.

4. Foreclosure by Powerful Supplier

There are circumstances in which RPM can lead to anticompetitive outcome without the involvement of multiple suppliers. The first one is when a powerful supplier uses RPM to foreclose rival suppliers by denying them access to effective distribution channels.[309] The supplier effectively uses RPM to generate quasi-rent to purchase exclusivity or privileged access to distribution channels.[310] This theory, however, only holds when a number of conditions apply. First, there must be a limited number of distribution channels or a scarcity of prime retail locations.[311] Otherwise, the supplier must be able to lock up a substantial portion of the distribution channels through its RPM scheme.[312] The RPM scheme must be able to generate sufficient quasi-rent to compensate the retailers for the loss of sales from other brands, which in turn depends on the supplier's market power. If the supplier was a monopolist, it would have very strong ability to generate such rent.[313] And since monopoly profit is greater than duopoly profit, a

305. *See id.* at 938 (explaining that if RPM is allowed, then "[t]here always exists a symmetric subgame perfect equilibrium in which wholesale prices are equal to cost . . . retail prices are at the monopoly level. . . retailers earn zero profit and manufacturers share equally the monopoly profit").

306. Patrick Rey, *Vertical restraints—an economic perspective,* FISCALÍA NACIONAL ECONÓMICA, 28 (Oct. 13, 2012), http://www.fne.gob.cl/wp-content/uploads/2013/11/Patrick-Rey.-Vertical-Restraints.pdf [https://perma.cc/WAS3-HULF].

307. Rey & Vergé, *supra* note 297, at 952-53.

308. *Id.* at 930.

309. *See* Elzinga & Mills I, *supra* note 270, at 360 (explaining that a manufacturer can use its RPM policy "to assure its retailers an attractive profit margin in implicit exchange for their deemphasizing or refusing to carry the goods of a competitor or new entrant").

310. *Id.*

311. Rey, *supra* note 306, at 31.

312. Elzinga & Mills II, *supra* note 294, at 1847.

313. *See* Ittai Paldor, *RPM as an Exclusionary Practice*, 55 ANTITRUST BULL. 309, 317-18 (2010) (explaining that monopoly rents are generally larger than duopoly rents, and that monopolies leave industries with larger profits).

monopolist would always be able to share some profit with a retailer to exclude a rival that leaves both the monopolist and the retailer better off.[314] RPM has effectively become "a rent-shifting device."[315] Meanwhile, the more crowded the market is at the upstream level, the less likely it is that the supplier will be able to generate sufficient quasi-rent to share with the retailers.[316] All this can be accomplished without an agreement. As Paldor observes, for supplier exclusion of rivals through RPM to work, there is no need for an express agreement; a tacit agreement suffices.[317] The supplier "may simply introduce RPM and rely on the incentives created by the system to assure that retailers carry only the incumbent's product."[318] This is the kind of unilateral behavior permitted by the *Colgate* doctrine.

5. Foreclosure by Powerful Dealer

Another circumstance in which RPM can hurt competition in the absence of multiple-supplier involvement is if it is used by a powerful dealer to forestall price competition at the retail level. This would be particularly pernicious if rivals were able to undercut the powerful dealer in price due to some innovation in distribution, the benefits of which RPM would prevent the rival dealer from passing on to consumers.[319] In order for the powerful dealer to forestall competition from more efficient dealers, it must be able to persuade the supplier to terminate those dealers. Again, one asks why the supplier would cooperate. The answer must be that the dealer possesses a significant degree of market power. Some of the conditions that are relevant to dealer cartels mentioned earlier would be equally relevant here. In order for the dealer to wield that much market power, alternative and equally effective distributors must have difficulty entering the market. In order for the powerful dealer to forestall competition and earn a supra-competitive profit, it needs to be able to eliminate more efficient rivals. After *Monsanto* and *Business Electronics*, all this could be very effectively achieved without exceeding the boundary of the *Colgate* doctrine and creating an illegal agreement.

314. *Id.* at 318.
315. *Id.* at 315.
316. *See id.* at 320 (asserting that when two, rather than one, competitors, exist, duopoly rents transform into "triopoly" rents, causing each firm's share of the rents to drop from one-half to one-third).
317. *Id.* at 343.
318. *Id.*
319. Elzinga & Mills I, *supra* note 270, at 360 (asserting that retail price increases caused by RPM policy increase total welfare — even though they may only provide greater surplus to some consumers — as long as the gains to some consumers are greater than the losses to other consumers).

6. Harm on Inframarginal Consumers

A supplier with some market power can cause consumer harm without attempting to foreclose rival suppliers or cartelize. This can happen simply because different groups of consumer have disparate preferences for sales and after-sales services. The idea that RPM can harm inframarginal consumers, even though it may benefit marginal consumers, originated from Michael Spence.[320] The key insight is that when a firm tries to expand sales, it only focuses on the marginal consumers.[321] However, the overall welfare effect of a firm's policy depends on its impact on both the marginal and the inframarginal consumers.[322] RPM may increase the welfare of the marginal consumers, but may reduce the welfare of inframarginal consumers by compelling them to pay a higher price for services that they do not need. Four conditions need to apply for this result to materialize:

> (1) [T]he manufacturer has some degree of monopoly power;[323] (2) marginal consumers value the services stimulated by RPM and increase purchases despite the higher price; (3) intramarginal consumers do not find the services worth the higher price; and (4) the decreased utility of intramarginal consumers exceeds the increased utility of marginal consumers.[324]

The inframarginal consumers are unlikely to be harmed in the presence of keen interbrand competition. They can simply switch to an alternative brand if they are dissatisfied with the unwanted service foisted upon them.[325]

The main idea is that marginal and inframarginal consumers have different preferences in terms of sales and after-sales services. Marginal consumers are those who are on the fence about purchasing the product, and may therefore be particularly sensitive to any changes in price or quality-adjusted price, which can be affected by the amount of sales and after-sales services.[326] Meanwhile, inframarginal consumers are those whose valuation of the product exceed the current price and thus do not need extra services to

320. A. Michael Spence, *Monopoly, Quality and Regulation*, 6 BELL J. ECON. 417,425 (1975).

321. William S. Comanor & John B. Kirkwood, *Resale Price Maintenance and Antitrust Policy*, 3 CONTEMP. POL'Y ISSUES 9, 14 (1985) ("[V]ertically motivated RPM always benefits marginal consumers.").

322. *Id.*

323. *Id.*

324. *Id*. at 15; *see also* Marvel & McCafferty, *supra* note 179, at 371.

325. Rey, *supra* note 306, at 13.

326. William S. Comanor, *Vertical Price-Fixing, Vertical Market Restrictions, and the New Antitrust Policy*, 98 HARV. L. REV. 983, 991 (1985) (explaining marginal and inframarginal consumers).

be enticed to purchase the product.[327] Raising the price to induce extra services will be a waste from the perspective of these consumers, who would prefer to pay a lower price for the product with less service.[328] Inframarginal consumers are likely to be knowledgeable consumers who do not require information and education at the store, while marginal consumers are likely to be relative novices to the product.[329]

Whether an RPM scheme harms consumers overall thus depends on whether the gain of marginal consumers is outweighed by the harm to inframarginal consumers, which in turn depends on the relative size of the two groups of consumers and the difference between their relative valuations of the underlying product.[330] Comanor argues that this means that there is a much weaker justification for RPM for established products, for which there is likely to be a higher proportion of knowledgeable consumers.[331] Note that the kind of consumer harm described here does not depend on how the RPM scheme is put in place. The same harm can result regardless of whether the RPM scheme is the result of a unilateral policy announcement or an illegal agreement.

B. *Economic Justifications for RPM*

A variety of justifications have also been offered for RPM. In fact, within the economics literature, there seems to be a greater number of articles justifying than condemning RPM. None of these justifications are premised on an RPM scheme being implemented through an agreement. They would equally apply to an RPM scheme enacted through a unilateral policy announcement.

1. Prevention of Free-Riding

This is probably the most well-known of the justifications for RPM. It was pioneered by Telser and has been elaborated and widely debated since.[332] The argument is probably too well rehearsed to warrant a full explanation here. The idea is that a supplier would like the dealers to provide services to

327. *Id.*
328. *Id.*
329. *Id.* at 992.
330. *See id.* at 999 ("A second question is whether the losses suffered by infra-marginal consumers are likely to outweigh the gains to marginal consumers. The answer depends on two related factors: the difference between the sizes of the two groups and the difference between their relative valuations of the underlying product.").
331. *Id.* at 1001.
332. Telser, *supra* note 268, at 89-96.

increase sales.[333] However, because of the difficulty in observing and verifying the provision of the services, the supplier cannot obtain these dealer services through a contractual arrangement.[334] The supplier could choose to let the dealers decide whether they want to provide the services on their own and let them charge a higher retail price to recoup the costs of providing the services. This, however, will not work because consumers will go to the full-service dealers to learn about the product and obtain product demonstration, and go to the no-frills dealers to purchase the product at cheaper prices. After a while the full-service dealers will realize that they are losing customers to the no-frills dealers and that it is no longer worth their while to provide the sales services the supplier wants. The no-frills dealers are said to be free-riding on the effort of the full-service dealers and the whole retail scheme unravels. The free-riding explanation does not apply to every product. Some products simply do not require any sales services. According to Telser, new branded products[335] and "old branded products purchased infrequently by relatively few households"[336] are the prime candidates for RPM.

Despite its widespread and intuitive appeal, some commentators have cast doubt on the applicability of the free riding explanation. In Telser's original conception, it was mostly applicable to sales services such as product demonstration. It has since been extended from sales services to after-sales services.[337] The free-riding explanation has much more limited validity with respect to after-sales services because the dealer can refuse to service a product it did not sell or charge separately for repair services.[338] Not every product requires sales services. Yet RPM has been observed in many products that do not require such services, such as candies, pet food, jeans, shampoo, etc.[339] It is mostly technically complex products that require such services. Therefore, even if free riding does provide an adequate justification for RPM, it only does so for a limited subset of products.

Apart from questioning the applicability of the argument to many products, commentators have also cast doubt on the link between higher retail margin and the provision of services desired by the supplier. Klein and Murphy argue that the free-riding explanation is "fundamentally flawed"[340]

333. *Id.*
334. *Id.* at 94.
335. *Id.* at 95.
336. *Id.* at 95.
337. *Id.*
338. *See* Grimes, *supra* note 255, at 476.
339. *See* Lao, *supra* note 207, at 80
340. Benjamin Klein & Kevin M. Murphy, *Vertical Restraints as Contract Enforcement Mechanisms*, 31 J.L. & ECON. 265, 266 (1988) (arguing that vertical constraints do not create incentives for competitive free-riding retailers to provide demonstration services, regardless of resale price maintenance practices).

because it is based on "the unrealistic assumption that the sole avenue of nonprice competition available to retailers is the supply of the particular services desired by the manufacturer."[341] Dealers may use the rent generated by RPM to supply services that are not wanted by the supplier.[342] In fact, nothing stops a dealer from enjoying the benefit of the extra retail margin generated by RPM and free-riding on other dealers' effort.[343]

Despite the divergent views on the validity of prevention of free-riding as a justification for RPM, what is clear is that none of these commentators have argued that the applicability of the defense is premised on the way in which the RPM is implemented. The effectiveness of RPM to prevent free-riding does not depend on whether the RPM scheme is achieved by unilateral policy announcement or an illegal agreement. As long as the dealers abide by the minimum resale prices, free-riding could be prevented.

2. Quality Certification

Marvel and McCafferty propose an alternative explanation for RPM. As opposed to prevention of free-riding, which requires retailers to provide tangible services, they argue that RPM is useful in inducing retailers that serve as quality certifiers in the eyes of consumers to carry the product.[344] These quality certifying retailers

> serve as their customers' agents, selecting from a wide variety of available merchandise those items [are] most likely to appeal to their clientele. By stocking a particular product on its shelves, the retailer attests that the quality and suitability of the item in question are consonant with the retailer's overall reputation.[345]

This explanation is only valid when the retailer's reputation is greater than the reputation of the product brand.[346] This could often be the case in the grocery market, where consumers are likely to be more familiar with the retailer, such as Whole Foods or Wal-Mart, than the brand name of a particular food item. It is less likely to be the case with well-known fashion brands such as Louis Vuitton and Chanel, which will not require quality certification, even by retailers as exclusive as Neiman Marcus and Bergdorf Goodman. Marvel and McCafferty themselves concede that this explanation

341. *Id.*
342. *Id.*; Robert Pitofsky, *In Defense of Discounters: The No-Frills Case for a Per Se Rule Against Vertical Price Fixing*, 71 GEO. L.J.1487, 1493 (1983).
343. *Id.*; *S\see generally* Grimes, *supra* note 255, at 483.
344. Marvel & McCafferty, *supra* note 179, at 347.
345. *Id.* at 348.
346. *Id.*

is likely to be particularly relevant to a new entrant.[347]

The question is what does the retailer provide in return for the greater retail profit margin. The greater return will be justified to the extent that quality certification entails significant costs, such as time and human resources needed to examine the products. This may be true for some products, such as food items, but may be less so for products whose quality can be readily observed. The greater return will also be justified if the retailer requires higher profit margin to maintain a better ambience or provide higher quality customer service to maintain the quality image.[348] RPM is necessary because otherwise consumers will observe the product at a quality certifying retailer, but proceed to purchase it at a cheaper retailer which does not sustain the costs of quality certification.

Scherer is among the most vocal critics of the quality certification justification. He raises three main criticisms of the justification. First, he argues that if consumers are unable to discern the quality of a product, they would be unable to know that products carried by a particular retailer are of high quality.[349] Second, Scherer doubts that a higher retail margin is necessary for the quality certifying retailer to recoup its costs. If the retailer is the first to sell the product, it will enjoy first-mover advantage and be the only retailer of the product for some time.[350] Finally, Scherer's more fundamental criticism of the justification is that quality certification amounts to a "status phenomenon,"[351] which means that consumers judge the quality of a product by the price level or by who else has bought the good.[352] This means that "the utility of diverse consumers is interdependent. And when the utility of consumers is interdependent, the whole foundation of welfare economics — that is to say, the branch of economics on which many of these judgments have been based crumbles."[353] Other commentators have also criticized this justification. Klein and Murphy argue that Marvel and McCafferty's prediction that new products are more likely to benefit from RPM does not comport with empirical evidence, which suggests that it is usually well-established brands that employ RPM.[354]

For our purpose, suffice it to note that nothing in Marvel and McCafferty's model requires the RPM scheme to be imposed by agreement.

347. *Id.* at 349.
348. *Id.*
349. *See* F.M. Scherer, *The Economics of Vertical Restraints*, 52 ANTITRUST L.J. 687, 695 (1983) (arguing that the Marvel and McCafferty explanation of discounter's impact on stores that certify high-quality goods is problematic and leaves a number of issues unaddressed).
350. *Id.*
351. *Id.*
352. *Id.*
353. *Id.* at 696.
354. Klein & Murphy, *supra* note 340, at 289.

The quality certification effect does not depend on the way in which RPM is implemented. In fact, Marvel and McCafferty compare dealer termination and RPM as alternatives for a manufacturer to implement quality certification, suggesting that the RPM scheme could be put in place simply by terminating non-compliant dealers.[355]

3. Facilitation of Contract Enforcement

Klein and Murphy propose yet another alternative justification for RPM. They argue that RPM is used not to avoid free-riding of sales services, but "to optimally compensate dealers on a per unit of sales basis for an increased supply of product promotion services and to prevent price competition that would eliminate the desired targeted marketing scheme."[356] They summarize their idea as follows:

> The manufacturer accomplishes this by creating an implicit contractual understanding with the dealer whereby the dealer agrees to provide the desired level of promotional services in exchange for a payment from the manufacturer. The contract is implicit because measurement problems prevent the manufacturer and dealer from contracting on the services directly. The payment may be made by the manufacturer with the use of vertical restraints such as an exclusive territory or resale price maintenance arrangement, . . . In any event, the manufacturer must always monitor dealer performance and terminate dealers who violate the implicit contractual understanding regarding the supply of promotional services.[357]

A manufacturer's RPM policy would serve as a contract enforcement mechanism to procure from retailers' non-contractible retail services that will boost the demand for the manufacturer's product. The RPM scheme creates quasi-rent, which entices dealers to provide the desired services.[358] Without the RPM scheme, the quasi-rent will be eroded by retail competition.[359] The manufacturer uses the quasi-rent stream as leverage over the dealers, which takes the place of contractual enforcement through the courts.[360] RPM saves the manufacturer time and effort to write a contract that exhaustively specifies the services required, often along dimensions that are difficult to articulate and measure.[361] If a dealer fails to perform the

355. Marvel & McCafferty, *supra* note 179, at 354.
356. *Id.*
357. *Id.* at 285.
358. *Id.* at 268.
359. *See* Mathewson & Winter, *supra* note 274, at 74.
360. Klein & Murphy, *supra* note 340, at 268.
361. *See* Elzinga & Mills II, *supra* note 294, at 1844.

desired services, it will be terminated and will cease to earn the quasi-rent.[362] Klein and Murphy argue that the quasi-rent stream need not represent supranormal return to the dealers. In the presence of manufacturer-specific investments, termination of a dealer would inflict sufficient pain on the dealer even if it was only earning normal profit.[363] However, they note that for RPM to serve its intended purpose, the quasi-rent created by RPM must exceed a dealer's short-run shirking potential,[364] which is what a dealer could hope to earn in the short run by not providing the requested services.

Paldor criticizes this justification for RPM as inadequate in that it will likely induce an insufficient level of service.[365] By using RPM to provide remuneration for retail services, dealers will be compensated on a per-unit basis.[366] Per-unit compensation is likely to under-compensate the dealers in light of diminishing returns to retail services and an upward-sloping supply for retail services.[367] Under-compensation means there will be an under-provision of services.[368]

Nothing in Klein and Murphy's model requires an agreement between the supplier and the dealers. In fact, the very essence of their model is that RPM will replace formal contracts to secure the necessary retail services. Enforcement of the RPM scheme only requires termination of non-compliance dealers to cut off their quasi-rent stream, which is precisely what is allowed under the *Colgate* doctrine.

4. Facilitation of Introduction of New Product

One of the justifications often offered for RPM is to induce dealers to carry a new product. The idea is that dealers may need to invest in the initial promotion of the new product. In the absence of RPM, subsequent dealers who did not incur such promotional expenses would be able to undercut the initial dealers and prevent the latter from recouping their investments.[369] Foreseeing this scenario, no dealers would agree to make the initial investments without RPM. This is one of the justifications for RPM that is accepted by both the majority and the dissent in the Supreme Court *Leegin*

362. Elzinga & Mills I, *supra* note 270, at 358.
363. Klein & Murphy, *supra* note 340, at 268.
364. *Id*. at 276.
365. *See* Paldor, *supra* note 313, at 331 (stating that retailers provide less than the desired level of service under the contract enforcement mechanism explanation).
366. *Id.*
367. *See id.* (noting that diminishing returns and an upward sloping supply are usually true).
368. *See id.* (concluding that dealers will be incentivized to provide fewer services).
369. Lao, *supra* note 207, at 76.

case.[370] In his dissent, Justice Breyer suggested creating an exception for new products employing RPM.[371] Despite the broad support this justification received in *Leegin*, it has been subject to a number of criticisms. It has been argued that vertical non-price restraints, such as exclusive territories, would be better suited for the purpose than RPM.[372] To the extent that the supplier itself can undertake the initial promotion, this justification for RPM crumbles. There are reasons to believe that the supplier can undertake much of the initial promotion itself.

5. Ensuring an Efficient Number of Outlets

RPM has been justified on the grounds that it can be used to induce retailers to open outlets in remote locations that will attract customers with high time costs.[373] The idea is that retailers need a higher margin to cover the costs of opening new outlets in remote locations, which would capture customers who otherwise would not have purchased the product.[374] Using RPM for this purpose entails a trade-off. On the one hand, a supplier would lose some sales from the higher retail price resulting from the RPM.[375] On the other hand, the supplier would gain sales from the improved availability of its product.[376] Whether it is worthwhile to use RPM to induce opening of more outlets comes down to whether the latter effect outweighs the former effect.

Three conditions are required for this use of RPM to be justified. First, the role of retailers is to reduce the consumers' time costs in obtaining the

370. *See* Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007) at 913, 917-18 (Breyer, J., dissenting) (explaining that both the majority and dissent credit this theory).

371. *See id.* (proposing that the per se rule be modified to include an exception because resale price maintenance facilitates the entry of new products, which is a consumer benefit).

372. Michael E. Jacobs, *Legal Treatment of Vertical Restraints: Some Lessons from the Ongoing International Debates,* FISCALÍA NACIONAL ECONÓMICA 17 (Oct. 25, 2012), http://www.fne.gob.cl/wp-content/uploads/2012/10/Legal-Treatment-of-Vertical-Restraints.pdf [https://perma.cc/EZ78-DVVR].

373. *See generally* J.R. Gould & L.E. Preston, *Resale Price Maintenance and Retail Outlets*, 32 ECONOMICA 302 (1965) (proposing that manufacturer may use RPM to induce retailers to open more outlets under the outlet hypothesis).

374. *See* Paldor, *supra* note 313, at 312-13 (explaining increasing the number of retail outlets as one potential justification for RPM).

375. *See* Calvani & Berg, *supra* note 9, at 1183 (observing that retailers with higher prices will lose some sales to price-sensitive consumers who can price shop at low-cost sellers); Mathewson & Winter, *supra* note 274, at 67 (stating that when all else is equal, a higher price results in a lower quantity sold).

376. *See* Mathewson & Winter, *supra* note 274, at 67 (noting that wider distribution can offset the loss from the higher prices of the protected margins).

product.[377] The product is the same no matter where it is bought. Second, retailers are differentiated in terms of their location and the time it takes consumers to search within a store.[378] Third, consumers have different opportunity costs of time.[379] Some consumers have very high search costs and would only purchase the product from a nearby store. Some consumers have low search costs and will travel long distances to purchase a product. Consumers with low search costs are likely to be more price sensitive, as they are willing to travel longer distances to save money. Therefore, when RPM is introduced, the trade-off is a balance between the number of new, high-search cost consumers attracted by the new outlets and the number of existing, low-search cost customers lost due to the higher retail price.

Winter argues that consumers with low search costs, who tend to have lower demand for the availability service at issue here, tend to be overrepresented in the retailer's calculus.[380] Thus when retailers try to accommodate the consumers' average preferences, they tend to focus on the low-cost customers who value low price and require low level of services.[381] Retailers tend to under-provide availability services and under-price their products.[382] Winter posits that this explanation for RPM should be most relevant for small-ticket items such as clothing, groceries, and drugs.[383] He also predicts that RPM should be most common "in markets or geographical areas in which the dispersion in income among consumers is the greatest. These markets, one can reasonably assume, have the greatest variation in opportunity costs of time."[384]

One obvious criticism of this justification is the huge discrepancy between the extra retail margin generated by RPM for small-ticket items, such as groceries and medication, and the enormous costs required to open a new outlet. Given that most supermarkets and drugstores carry hundreds, if not thousands, of brands, a higher retail margin on one brand will have a negligible impact on the overall profitability of the store, let alone generate enough revenue to open a new store. Therefore, a majority of brands sold in

377. Ralph A. Winter, *Vertical Control and Price Versus Nonprice Competition*, 108 Q.J. ECON. 61, 62 (1993).

378. *Id.*

379. *Id.*

380. *See id.* at 63 (explaining that retailers often overlook the customers whose high time costs prevent them from buying the product and instead focus on consumers with low time costs who do not need services).

381. *Id.*

382. *See id.* (noting that retailers focus on consumers who have a low demand for services and, thus, rely on low prices to attract customers).

383. *See id.* at 70 (stating that the service provided for small-ticket items is shelf space, but the customers willing to shop in stores are the least influenced by shelf space since they have the time to shop carefully).

384. *Id.* at 70-71.

supermarkets and drugstores must simultaneously practice RPM for this justification to hold. The free-rider problem here is obvious. If each brand accounts for a negligible proportion of the overall profit of the store, it will have overriding incentives to cheat and free-ride on the retail margin generated by other brands. Given the multitude of brands that need to be monitored, it will be extremely costly to police against free riding. Therefore, one may argue that this justification verges on unrealistic.

For our present purpose, suffice it to note that nothing in this justification requires the RPM scheme to be implemented through an agreement. As long as the retailers follow the minimum resale prices, the intended effect of inducing the opening of more outlets will be produced. It matters not whether the RPM scheme is implemented by unilateral policy announcement or an illegal agreement.

None of the main theories of harm and economics justifications for RPM are premised on the existence of an agreement. The economic effects of the conduct will materialize as soon as the dealers abide by the supplier's wishes, and vice versa.[385] As Robinson observes, "the *form* of the vertical arrangements between manufacturer and dealer is irrelevant. The existence of a vertical agreement has no evidentiary significance on whether to accept the benign or malign account because it is entirely consistent with either."[386] The agreement requirement adds nothing to the economic analysis and merely serves to obscure its focus. There are thus no coherent economic justifications for an agreement requirement.

V. PRACTICAL JUSTIFICATION FOR AN AGREEMENT REQUIREMENT

One practical justification for an agreement requirement and retaining the *Colgate* doctrine is that the doctrine serves as a safe harbor for firms that wish to institute RPM schemes while avoiding litigation. Before *Leegin*, the consequences of exceeding the doctrine were dire as it would result in *per se* illegality. After *Leegin*, the RPM scheme would not be subject to summary condemnation but would be examined under the rule of reason. If a firm wishes to avoid any litigation at all, it could do so by staying within the confines of the *Colgate* doctrine.

The reality is that the *Colgate* doctrine has provided a very costly and byzantine safe harbor for firms to navigate. Given the highly complex and

385. *See generally* Burns, *supra* note 61, at 32 (noting that whether a vertical agreement is legal does not depend on the distinction between an agreement and a unilateral action); Grimes, *supra* note 255, at 491 (stating that there must be interaction between the dealers and suppliers, so the effects should be determined by whether the vertical integration is anticompetitive or procompetitive).

386. Robinson, *supra* note 24, at 597-98.

at times contradictory Supreme Court case law on the *Colgate* doctrine, administering a compliant RPM system requires detailed and constant legal advice. Henry and Zelek, Jr. produced a detailed practical guide on how to implement an RPM scheme under *Colgate*.[387] In order to stay within the *Colgate* doctrine, a firm must exercise caution in choosing whom to involve in the RPM scheme. The scheme should only apply to dealers that deal directly with the supplier and not to downstream dealers.[388] A decision has to be made as to whether to adopt the same or different policies with respect to the resellers and the wholesalers, which may produce different legal consequences.[389] Suppliers can also choose to minimize legal risks by attempting to recast wholesalers as agents and by instituting an authorization policy for resellers.[390] Under this policy, wholesalers can only sell to authorized resellers. If a reseller violates the unilateral policy announcement, the wholesalers are notified that they can no longer supply that reseller.[391]

Communication with the dealers needs to be handled with care. At no point should the supplier be seen as seeking commitment to comply with the unilateral policy.[392] The authors recommend a centralized administration structure that reports directly to the management to administer such a scheme.[393] They emphasize the importance of providing adequate training to employees who interact with the dealers on a regular basis.[394] They also advise that:

> [A]ntitrust counsel, whether inside or outside, be assigned to work closely with the administrator or the administration team. In the early stages of policy implementation, it is not uncommon for teams to meet several times each week to consider issues that arise during implementation, but that could not have been realistically

387. *See* Brian R. Henry & Eugene F. Zelek, Jr., *Establishing and Maintaining an Effective Minimum Resale Price Policy: A Colgate How-to*, 17 ANTITRUST 8, 9 (2003).

388. *See id.* at 10 (providing that sales directly from supplier to dealer satisfy the requirement that resale price policies be unilaterally imposed).

389. *See id.* (proposing that a business's needs and a supplier's capabilities should influence whether the policy adopted applies only to resellers or to both resellers and wholesalers).

390. *See id.* at 11 (explaining two additional ways to alter the relationships between the supplier and resellers).

391. *Id.*

392. *See id.* at 12 (describing a requirement for unambiguous language which communicates that suppliers are not pursuing reseller's agreement to follow a unilateral policy).

393. *See id.* (highlighting uniformity and consistent reporting to senior management as benefits of centralizing the policy administration).

394. *See id.* at 14 (asserting the need for anyone who communicates with dealers to obtain antitrust and policy education).

foreseen in the planning process.[395]

The authors also provide detailed guidance on what the supplier can and cannot do to monitor compliance and handle dealer complaints. Suppliers are told not to rely exclusively on complaints from other dealers.[396] In particular, suppliers are cautioned not to have any conversations regarding a dealer's pricing intentions, but "must walk a fine line in unilaterally assessing the retailer's intent and making the policy violation termination."[397] The authors even suggest the use of marketing research firms, accounting firms, or detective agencies to help monitor dealer compliance.[398] Doing so would substantially increase the costs of the scheme. It is not even clear that reliance on agents to police an RPM scheme is allowed under *Parke* and *Albrecht*. If a dealer has been found to have violated the scheme, the letter notifying of the termination "must be carefully crafted"[399] to avoid giving any impression that the supplier is seeking reassurance of future compliance from the dealer. Lastly, the authors point out that reinstatement of terminated dealers is fraught with difficulty and must be handled with extreme care.[400]

In its study of the use of RPM in the contact lens sector, the American Antitrust Institute ("AAI") notes similar difficulties in the implementation of a unilateral RPM policy.[401] The authors of the study refer to the "management issues associated with unilateral price policies"[402] and note that such policies "are challenging to develop and adopt and costly to monitor and enforce."[403] They further conclude that as a result of the management challenges, a unilateral RPM policy is "typically harder to control and less efficient."[404]

A recurrent theme in the detailed advice from Henry and Zelek and the

395. *Id.* at 12.

396. *See id.* at 13 (warning that legal and business risks will befall the supplier who relies exclusively on complaints from other dealers).

397. *Id.*

398. *See id.* (explaining how the credibility problems associated with dealer-sourced complaints can be mitigated through audit programs, with a more formal program including the use of market research companies, accounting firms, or detective agencies performing mystery shops or audits of dealer records).

399. *Id.*

400. *See id.* (describing how suppliers must determine whether, and when, to reinstate dealers and how the Sherman Act prevents this reinstatement from being conditional on compliance with the policy in the future).

401. Gregory T. Gundlach & Riley T. Krotz, *Resale Price Maintenance After* Leegin*: The Curious Case of Contact Lenses* 25 (Am. Antitrust Inst., Working Paper No. 15-04, 2015), http://www.antitrustinstitute.org/sites/default/files/AAI%20working%20paper%2015-04.pdf [https://perma.cc/3QRE-APBL] (concluding that unilateral RPM is difficult to develop and costly to monitor).

402. *Id.*

403. *Id.*

404. *Id.* at 26.

AAI study is difficulty of implementation and the care with which implementation must be handled. Brunell observes that the *Colgate* doctrine "only pushes manufacturers that wish to set retail prices to adopt wasteful or seemingly irrational measures"[405] and is "too draconian and costly a weapon to use to combat discounting."[406] RPM is one of the few areas of antitrust law where the implementation details of the conduct requires such extensive counseling. It is one of the few areas of antitrust where legality turns on not whether particular conduct took place but how it was implemented.

The result of such specific and detailed requirements of a legal RPM scheme under *Colgate* is very high administration costs. Hinman and Shah note that the need to comply with *Colgate* means that "monitoring and enforcing a unilateral policy can impose significant costs on a manufacturer."[407] The golf club company Ping reportedly spends several million dollars per year and devotes as many as twelve full-time employees to administer its RPM scheme.[408] The staggering costs and human resource requirements led Grimes to conclude that "the Colgate defense requires 'legal gymnastics' that are costly, disruptive to dealer-manufacturer relations, and have no relevance to the procompetitive or anticompetitive effects of the underlying practice."[409]

While the *Colgate* doctrine arguably still served a purpose when the *per se* rule prevailed, it is clear that the convoluted body of case law under the doctrine has become a needless distraction from the crux of the issue, which is the competitive effects of the restraint. The safe harbor that it allegedly provides to firms is costly and immensely complicated to navigate. It is beset with uncertainty as a single misstep can cause the whole scheme to unravel. The entire area of law would be much improved if, instead of relying on a form-based safe harbor such as the *Colgate* doctrine, substantive safe harbors based on market power and perhaps the origin of the scheme are used.

VI. THE PROPOSAL

A. *The Colgate Doctrine and the Agreement Requirement*

It should come as no surprise that this Article advocates the abolition of the agreement requirement for vertical restraints. From the perspective of

405. Richard M. Brunell, *Overruling Dr. Miles: The Supreme Trade Commission in Action*, 52 ANTITRUST BULL. 475, 523 (2007).

406. *Id.* at 524.

407. Frank M. Hinman & Sujal J. Shah, *Counseling Clients on Vertical Price Restraints*, 23 ANTITRUST 60, 62 (2009).

408. *See* Grimes, *supra* note 255, at 489 (illustrating the high cost of implementing an RPM scheme and the extent to which dealers are terminated).

409. *Id.* at 490.

the purpose of an agreement requirement, it has been argued that the requirement is most justified as an identification device to discover conduct that is the subject of possible antitrust condemnation. This identification device should accord the same treatment to conduct that produces the same economic effects. In the context of horizontal restraints, the agreement requirement arguably serves a useful function because it distinguishes between permissible parallel pricing and illegal collusive conduct. In the context of vertical restraints, however, there is no overriding reason to condone unilaterally imposed RPM but condemn mutually agreed RPM. Both kinds of RPM produce the same economic effects and may benefit from the same justifications. Therefore, the agreement requirement does not serve a useful function in the vertical restraint context.

The various theories of agreement under the *Colgate* doctrine are logically incoherent and theoretically unsound. They also fail to provide meaningful and clear guidance on the boundary between permissible unilateral conduct and illegal concerted action. This means that the agreement requirement does not even perform the function that it purports to serve. Furthermore, the agreement requirement makes no contribution to the ultimate issue in the analysis, the competitive effects of RPM. None of the main economic theories of harm and justifications for RPM are premised on the existence of an agreement. This means that the abolition of the agreement requirement will make no difference in the substantive analysis. So long as the supplier demands the observation of minimum resale prices and the dealers comply, the economic effects of RPM, both good and bad, will materialize.

The argument for doing away with the agreement requirement is even stronger after the abolition of the *per se* rule in *Leegin*. While the *per se* rule still applied, the Court tried to use the agreement device to distinguish anticompetitive uses from pro-competitive uses of RPM. The agreement requirement and the related *Colgate* doctrine took on a substantive function. With the *per se* rule overruled by *Leegin*, this commingling of formal and substantive issues no longer seems justified.[410] The sharp distinction between vertical price restraints and vertical non-price restraints maintained in *Business Electronics* is also no longer warranted. The abolition of the *per*

410. *See* Hovenkamp, *supra* note 24, at 6 ("Under the rule of reason such strictness is no longer necessary because anticompetitive effects are no longer inferred from the price agreement alone."); *see also* Harrison, *supra* note 92, at 1144 (explaining how moving away from per se treatment focuses the analysis on competitive effects); Grimes, *supra* note 255, at 491 (praising a rule of reason which considers the substantive competitive effects rather than the supposedly unilateral form of the agreement); Robinson, *supra* note 24, at 601-02 (discussing how the per rule was based on formalistic, rather than substantive, assumptions); Hay, *supra* note 10, at 440 (arguing that the issues of the form of agreement under Colgate would no longer be as important under a rule of reason).

se rule also calls for a new perspective on the legality of dealer termination.

One obvious objection to abolishing the agreement requirement is that it is a statutory requirement, or at least a requirement supported by decades of case law. Section 1 of the Sherman Act only applies to agreements. Short of a statutory amendment or drastic turn in the case law, the agreement requirement is here to stay. It is possible to unofficially abolish the agreement requirement without either development: to overturn the *Colgate* doctrine. The *Colgate* doctrine can be said to consist of two components. The first part is the right of a supplier to implement an RPM scheme through unilateral policy announcements without exposing itself to antitrust scrutiny. The second part is the right of a supplier to terminate a non-compliant dealer. The second part will be discussed in greater detail below. As for the first part, if the *Colgate* doctrine was abolished, it would mean that an RPM scheme implemented through unilateral policy announcements would also be deemed to be agreements within the reach of Section 1. This position is relatively uncontroversial as quite a number of commentators have argued that the kind of conduct sanctioned by the doctrine amounts to an implied contract under contract law and therefore would most certainly constitute an agreement.[411] If even the kind of conduct sanctioned by the *Colgate* doctrine is deemed to be an agreement, there is probably no way for a supplier to implement an RPM scheme while staying beyond the reach of Section 1. A supplier cannot implement an RPM scheme with less interaction with the dealers than what is currently allowed by the *Colgate* doctrine. Eliminating the *Colgate* doctrine means that every RPM scheme contains an agreement, which is no different from saying that an agreement is no longer required to establish an illegal RPM scheme. While formally abolishing the agreement requirement would be an intellectually more honest way to proceed, overturning the *Colgate* doctrine would produce the same result.

B. *The Consignment Exception*

Even though the consignment exception strictly speaking is not related to the agreement issue — in consignment cases, there is no doubt that there are agreements, the question is whether these agreements should somehow be exempted because they involve consignment — it should also be considered in this Article because it is similarly concerned with how form

411. *See* Harrison, *supra* note 92, at 1134 ("Under basic contract law principles, the outcome could easily be squared with the existence of an implied agreement."); *see also* Robinson, *supra* note 24, at 587 (arguing that it is odd to refer to the supplier-dealer relationship as something other than an implied contract); Pitofsky & Dam, *supra* note 223, at 774 (demonstrating that a tacit agreement can be found even when the dealer is able to prove coercion).

trumps substance in the antitrust analysis of RPM. Unsurprisingly, just as this Article suggests that the agreement requirement be abolished, it recommends the same fate for the consignment exception. The reasons are similar to those supporting the abolition of the agreement requirement. Substantive issues have similarly seeped into the formal issue of whether there is a bona fide consignment agreement. It has been argued that the kind of analysis undertaken in *Simpson* is reminiscent of a rule of reason analysis.[412] Similar to the agreement issue, where the existence of an agreement makes no substantive difference, whether a dealer is a bona fide agent or an independent reseller has no bearing on the substantive effects of the conduct.[413] As Harrison argues, "[a]s long as independent business entities are involved, the issues of price and sham agencies become irrelevant. . . . The overarching question would remain whether the arrangement has an undesirable effect."[414] Therefore, the consignment exception should be abolished, ending the confusion about the state of the law with the conflicting *General Electric* and *Simpson* opinions. Instead, the analysis should focus on whether the arrangement produces consumer harm and is otherwise justified by pro-competitive benefits.

C. *Dealer Termination*

One suggestion put forward earlier is the decoupling of dealer termination from vertical price fixing and treating dealer termination as a possible independent antitrust violation. This means that regardless of whether there is a concomitant RPM scheme, dealer termination could constitute an antitrust violation if certain conditions are met. This, however, does not mean that every dealer termination is illegal under antitrust law. It was mentioned earlier that there are two components to the *Colgate* doctrine, the second of which being that a supplier has the right to terminate a non-compliant dealer and the right to choose with whom it will deal. Despite the proposed abrogation of the first component of the doctrine, the second component should be maintained. One reason that the *Colgate* doctrine has outlasted the *per se* rule in *Dr. Miles* is the great intuitive appeal of the notion that a supplier should have the freedom to choose with whom it will deal. There is no reason that a supplier's trader freedom should be any greater or smaller than any other business. If this freedom is unduly restricted,

412. *See* Harrison, *supra* note 92, at 1153 (finding that the analysis in *Simpson* reflects a rule of reason analysis because it focuses on substantive impact, rather than formalistic labels).

413. *See id.* at 1152 (describing the classification of a dealer as a bona fide or sham agent as formalistic and irrelevant after *Leegin*).

414. *Id.* at 1153.

suppliers will simply be more hesitant to enter into relationships with dealers. But such freedom should not be unfettered. It should be subject to the usual strictures of antitrust under which dealer termination that harms consumers will be prohibited. What this means is that at the very least, dealer termination should be subject to the law on unilateral refusal to deal under Section 2. This is consistent with the intention of the *Colgate* court, which qualified the *Colgate* right of termination by the caveat that the right only applies "[i]n the absence of any purpose to create or maintain a monopoly."[415] A dealer termination should only fall within the ambit of Section 2 if it is a genuinely unilateral decision. This means that the supplier would have terminated the dealer anyway regardless of other factors, such as complaints by other dealers. Given the stringent standard imposed by the Supreme Court on a unilateral refusal to deal claim in *Trinko*,[416] the reality is that very few plaintiffs will successfully invoke Section 2 to challenge dealer termination.

For dealer termination that is not genuinely unilateral, the focus of the analysis should not be on whether there is an agreement between the supplier and the complaining dealer either to adhere to minimum resale prices or to terminate the offending dealer. The existence of an agreement adds nothing to the analysis. What matters is whether the supplier would have terminated the offending dealer but for the dealer complaint. If the supplier would not have terminated the offending dealer but for the complaint, there is a prima facie claim that the termination is anticompetitive.[417] The plaintiff can meet its burden of proof under the but-for standard by showing that it was terminated because of its price cutting and it was plausible that the supplier would have terminated the plaintiff in response to complaints by another dealer because the latter dealer's business is more important to the supplier. And if the supplier fails to furnish alternative reasons for the termination, the plaintiff will have a valid dealer termination claim. The question is whether this should be the end of the inquiry or whether further showing of competitive effects should be required. In other words, whether dealer termination should be *per se* illegal once it is proven that it was impelled by

415. *Colgate*, 250 U.S. at 307.

416. *See* Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko, 540 U.S. 398, 408-9 (2004) (recognizing the limited circumstances under which a unilateral refusal to deal may constitute an anticompetitive act).

417. *See* Hovenkamp, *supra* note 24, at 13 ("Further, termination responses reflecting the manufacturer's own distribution policy differ greatly from those imposed upon it by a complaining dealer. In the latter case, the manufacturer's compliance with the complainer's demand is more likely to be anticompetitive."). *But see* Floyd, *supra* note 18, at 273 ("Thus, termination of a price-cutting distributor following receipt of price complaints, even if the complaints are the 'but for' cause of the termination, is not by itself a violation of the Sherman Act.")

dealer complaints.

Despite contrary arguments by some commentators,[418] the rule of reason should prevail. There are two reasons for this. First, commentators who suggested that the *per se* rule should apply did so when the *per se* rule still applied to RPM. This is no longer the case. The overturning of the *per se* rule for RPM does not necessarily mean that the *per se* rule cannot apply to complaint-motivated dealer termination. RPM and dealer termination need not be subject to the same legal standard. If one focuses on competitive effects, however, it is clear that complaint-motivated dealer termination cannot produce greater harm than a supplier-imposed RPM scheme. The most that such termination can do is produce price uniformity at the dealer level for a particular brand. The extent to which such uniformity can harm consumers depends on the extent of interbrand competition. If interbrand competition is keen, consumers are unlikely to be harmed by the unilateral exercise of market power by one dealer under one brand. Second, once one does away with the agreement requirement for dealer termination, a complaint-motivated dealer termination is nothing more than what Judge Posner describes as a unilateral exercise of market power. The powerful dealer is effectively demanding exclusivity if it exercises its market power to the limit and eliminates every competitor. If exclusive dealing is subject to the rule of reason, there is no reason that complaint-motivated dealer termination should be subject to a more stringent rule.

Under the rule of reason analysis, dealer termination would only be illegal if interbrand competition is sufficiently weak that the decimation of intrabrand competition through dealer-driven dealer termination would have an impact on the relevant product market. So long as interbrand competition is keen, the elimination of intrabrand competition through dealer-driven dealer termination would not harm consumers and should not be condemned by the antitrust law.

The analysis would be different if multiple dealers come together to pressure the supplier to terminate a price-cutting dealer.[419] In that case, it would no longer be a unilateral exercise of market power. Regardless of whether there is an agreement among the complaining dealers, the dealers are aggregating their market power to coerce the supplier to do something which they individually would not be able to accomplish. This would be

418. *See* Thomas A. Piraino, Jr., *Distributor Termination Pursuant to Conspiracies Among a Supplier and Complaining Distributors: A Suggested Antitrust Analysis*, 67 Cornell L. Rev. 297, 397 (1982) (expressing that courts fail to consider the use of the per se rule for dealer terminations induced by a single dealer when they apply the rule of reason on the basis of the vertical form of the conspiracies).

419. *But see id.* at 319-320 (proposing a two-step analysis in mixed termination cases that requires the existence of an agreement between the supplier and dealer and considers the supplier's competitive purpose for entering the agreement).

analogous to a group boycott.[420] Under *Northwest Wholesale Stationers*, such boycott would be *per se* illegal if it could be shown that the group possesses market power.[421] And if the dealers acting in concert managed to coerce the supplier to terminate a price-cutting dealer, the dealers are likely to possess the requisite amount of market power for the purpose of *Northwest Wholesale Stationers*.

CONCLUSION

The abrogation of the *Colgate* doctrine is the logical conclusion of the rule of reason revolution in vertical restraints. After *Leegin* introduced the rule of reason for RPM, there is no longer any reason to rely on the agreement requirement as a proxy for competitive harm and to soften the blow of the *per se* rule. A formal requirement such as an agreement is not the right place for substantive analysis, as it becomes necessary to pigeonhole substantive elements into the strictures of a formal device. This has led the courts to focus on tangential issues such as the degree of coercion and the extent of enforcement effort that have nothing to do with the ultimate inquiry of the competitive effects of the conduct. With the rule of reason, it is now possible to undertake a full-fledged substantive analysis independent of the formal requirement. The agreement requirement no longer serves a useful purpose as an agreement is not necessary to locate the locus of competitive harm. What matters is not whether an RPM was implemented by an agreement, but whether an RPM was implemented.

In fact, abolishing the *Colgate* doctrine is merely aligning RPM with other vertical restraints such as tying and exclusive dealing, where the unilateral conduct defense has never played a prominent role.[422] This is especially true in tying cases, where the tie is often unilaterally imposed by the defendant, and the agreement at issue is simply the sales agreement between the parties.[423] This approach is more consistent with the Posnerian view that vertical restraints are simply a unilateral exercise of market power.

420. *See* Levi, *supra* note 9, at 269-70 (stating that illegal boycotts may be created when wholesaler refuses to deal with retailers that adjust prices).

421. *See cf.* Nw. Wholesale Stationers v. Pac. Stationery & Printing Co., 472 U.S. 284, 296 (1985) (stating that the immediate conclusion of an anticompetitive effect is not warranted unless the group has market power or access to an important competitive input).

422. *See* Robinson, *supra* note 24, at 590 (arguing that the unilateral action defense is rarely used due to the Supreme Court's failure to provide an instruction on the matter).

423. *See id.* (adding that the unilateral action defense is often ignored in tying cases where the tie is unilaterally opposed by the seller on the buyer and the Colgate defense is applicable); Grimes, *supra* note 255, at 489 (asserting that the likelihood of dealers participating in resale price maintenance is higher than in tying cases, even though downstream buyer's compelled acceptance of the tie suffices to establish an agreement).

It is curious that given tying is also subject to the *per se* rule, albeit a qualified one under *Jefferson Parish*,[424] the courts have not extensively deployed the same tactic and softened the *per se* rule with a unilateral conduct defense. This could be because with tying the courts have instead turned to softening the substantive rule with the qualified *per se* rule.

One may question whether the agreement requirement serves any useful purpose for vertical restraints. This is not to say that an agreement never exists in vertical restraints. There are probably some vertical restraints that are so complex that they cannot be put in place and implemented without an agreement between the supplier and the dealers. But this does not mean that the finding of an agreement aids the analysis or helps to determine the legality of the restraint. The only circumstance in which the finding of an agreement arguably serves this purpose is in the horizontal context, where the agreement concept is used to identify illegal price fixing among parallel pricing situations. Even this view has been persuasively questioned by Kaplow. Kaplow, however, stops short of advocating the abolition of the agreement requirement in the horizontal context, arguing that more careful studies need to be done.[425]

A wholesale abolition of the agreement distinction between Section 1 and Section 2 of the Sherman Act is beyond the scope of this Article. It does have certain intuitive appeal, as there are persuasive arguments that what separates unilateral action from concerted conduct is not whether there is an agreement between the parties, but whether their market power is being directed to a common purpose. One difficulty with the abolition of the distinction is that it may allow antitrust scrutiny of unilateral conduct when the party at issue possesses less than monopoly power. Some have said that unilateral exercise of market power by non-monopolists is a gap in the current antitrust jurisprudence, while others have argued that it is a valuable distinction worth preserving. Resolving this argument probably requires further research and careful analysis. What remains true is that the de-emphasis of the agreement requirement is a sensible development in antitrust as its focus shifts further away from form to substance. Modern antitrust has always been about substance, and not form. The form in which the conduct takes place matters much less in the analysis than the substantive impact of the conduct. This is especially true in the RPM context where the analysis of the formal issues has become so convoluted that it has obscured the

424. *See* Jefferson Par. Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 3 (1984), *abrogated by* Ill. Tool Works Inc. v. Indep. Ink, Inc., 547 U.S. 28 (2006) (holding that tying should only be condemned if it restrains competition by forcing purchases that would otherwise not be made).

425. *See* Kaplow, *supra* note 165, at 813-14 (concluding that price-fixing prohibitions create doubts about abolishing the agreement requirement in the horizontal context such that additional analysis is required).

substantive analysis.