



US Supreme Court overturns ruling on RPM agreements

LEEGIN CREATIVE LEATHER PRODUCTS, INC. V PSKS, INC.

This briefing examines the recent US Supreme Court ruling in *Leegin Creative Leather Products, Inc. v PSKS, Inc.*, in which the Court overturned its nearly 100 year old ruling on resale price maintenance agreements in the *Dr. Miles* case.

On 28 June, the US Supreme Court (the Court) overturned its nearly 100 year old ruling in the *Dr. Miles* case, which made resale price maintenance (RPM) agreements per se unlawful. In *Leegin Creative Leather Products, Inc. v PSKS, Inc.*, the Court ruled that RPM agreements in which a manufacturer sets the minimum price for a product should be evaluated under the rule of reason standard. Although RPM agreements are still subject to scrutiny to determine whether, on the weighing of all factors, they harm competition, this ruling should simplify negotiation and enforcement of distribution agreements. The decision obviates the need for the parties to engage in the many 'work arounds' to the *Dr. Miles* rule that evolved in an effort to achieve the same legitimate business purposes as can now be served directly by an RPM agreement.

Details of the case

In this case, a jury found that the manufacturer, Leegin, had stopped selling its leather fashion accessories to retailer PSKS because PSKS sold the Leegin products below 'suggested' retail prices. The jury found that this termination of PSKS for selling below suggested prices was illegal RPM and awarded PSKS \$1.2m in damages. As RPM was per se illegal, Leegin was not permitted to argue that its sales programme enhanced interbrand competition and had the legitimate purpose of encouraging its retailers to devote resources to selling its products. The Court of Appeals reasoned that it was bound to follow the Court's *Dr. Miles* precedent and affirmed the jury's verdict.

Supreme Court ruling

In a 5-4 ruling the Court overturned *Dr. Miles* and held that minimum RPM should be analysed under the rule of reason, a multifactor test that requires 'the fact finder to weigh all of the circumstances... including specific information about relevant business and the restraint's history, nature and effect'. Analysis of RPM under the rule of reason follows earlier decisions applying the rule of reason to maximum RPM and non-price vertical agreements (*State Oil Co. v Khan*, 522 U.S. 3 (1997)).

In its decision the Court cited the need to keep the Sherman Act current in its relevance to the 'dynamics of present economic conditions' and noted that the economic literature supports a finding that a per se rule is inappropriate for a scheme that is not always anticompetitive in effect. The Court noted that RPM schemes promote 'interbrand competition among manufacturers selling different brands of the same type of product by reducing intrabrand competition among retailers selling the same brand', but cautioned that potential anticompetitive effects of RPM should not be 'ignored or underestimated'. Successful challenges to RPM agreements will need to show that the agreements raise prices, limit consumer choice, enhance monopoly power or facilitate cartel conduct.

The Court instructs lower courts to consider factors including the number of manufacturers that have also adopted the scheme, their market power and the source of the restraint. The Court notes that RPM in high-price, high-service brands 'encourages retailers to invest in

tangible or intangible services or promotional efforts that aid the manufacturer's position as against rival manufacturers and is therefore likely to be found reasonable'. Conversely in low-price, low-service brands, there are likely to be fewer legitimate business purposes for setting a minimum price for such commodities.

Implications

Although *Leegin* reverses the rule that RPM is per se illegal under the federal Sherman Act, state courts may choose to interpret their own antitrust statutes differently. For example, courts are not required to interpret California's antitrust statute, the Cartwright Act, in the same manner as the Sherman Act and may choose to continue to adhere to the per se rule from *Dr. Miles*.

Despite some uncertainty, the *Leegin* decision simplifies both negotiation and enforcement of US distribution agreements. RPM provisions are now subject to the same lenient rule of reason standard that applies to all other vertical restraints. RPM agreements may therefore be negotiated and enforced with diminished risk of antitrust challenges being brought by retailers or consumers. Manufacturers would be well-advised to document the business purpose for RPM in distribution agreements, especially manufacturers with substantial market share or those in 'low-price, low-service' markets. Finally, as with all vertical agreements, manufacturers should avoid RPM agreements that effect a horizontal agreement. Courts and enforcement agencies will closely scrutinise RPM agreements that appear to be the result of (i) a horizontal agreement between resellers seeking to maintain high resale prices or (ii) a horizontal agreement between manufacturers to facilitate price fixing.

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