

## Supreme Court Abandons Absolute Prohibition on Price Floors

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For nearly a century, it has been illegal for a publisher or other manufacturer to make an agreement with a retailer as to the discount at which the retailer may sell the publisher's products. A month ago, in a 5-4 decision, the Supreme Court overruled its 1911 decision in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, thereby removing the rule that such "resale price maintenance agreements" are always (or, "*per se*") illegal. Under the Court's recent opinion in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, resale price maintenance agreements will now be reviewed under a "rule of reason" analysis which evaluates whether the particular arrangement is anticompetitive, rather than treating all such agreements as illegal.

What does this decision mean for publishers? Are publishers now free to require that retailers sell their books at full retail price, or to set a maximum discount at which they may be sold? And why would publishers desire the flexibility to manage retail prices?

Economists have suggested for years that resale price maintenance programs can create positive economic benefits by, among other things, eliminating "free riding" by low-price discount retailers that co-opt sales from higher-priced, full-service retailers. This can occur, particularly on expensive products, when a customer receives a recommendation regarding a product from their local retailer, but then purchases the product at a lower price from an online retailer that does not have the overhead cost of maintaining and training staff that can recommend such products. Some publishers, particularly curriculum publishers, would like to apply this reasoning to address price-competition by discount retailers. When competition is focused on price, the reasoning goes, the resulting reduced margins can drive out the ability of "full-service" Christian bookstores to invest in the staff to educate pastors and other consumers regarding backlist titles and curriculum.

At this point, the impact of the *Leegin* decision is unclear, and will remain unclear until lower federal courts interpret which types of resale price maintenance agreements are acceptable under the rule of reason analysis. But, for publishers evaluating whether to explore a resale price maintenance program, reviewing the background of the *Leegin* decision is instructive. The following lengthy excerpt about the case is drawn from an article by experienced antitrust lawyer Alan S. Middleton at Davis Wright Tremaine LLP:

"In *Leegin*, defendant Leegin Creative Leather Products manufactured, distributed, and marketed leather goods and accessories under the Brighton brand. It sold its merchandise primarily through small, independent retail outlets. Leegin believed that small retailers offered better service and a better overall purchasing experience to the customer than

large national chains. Plaintiff PSKS operated Kay's Kloset clothing stores. Leegin introduced a policy under which it refused to sell to retailers who sold its products below suggested prices. It wanted its retailers to earn a sufficient margin to cover the cost of providing better customer service. Leegin then asked its retailers to pledge to sell its products at suggested prices. Kay's Kloset refused to stop discounting; Leegin therefore stopped selling its Brighton line to the store. The retailer sued based upon the *per se* rule of *Dr. Miles* and prevailed both in the trial court and before the Fifth Circuit, winning a verdict of \$1.2 million (trebled under the antitrust laws).

"The case attracted much attention. The U.S. Department of Justice and Federal Trade Commission filed a brief supporting reversal of *Dr. Miles*. The New York Antitrust Bureau opposed reversal. FTC Commissioner Pamela Harbour wrote an open letter to the Court urging it not to overrule *Dr. Miles*. Several industry groups, including CTIA-The Wireless Association, the National Association of Manufacturers, and the American Petroleum Institute, filed briefs in support of Leegin.

"In the majority decision, the Supreme Court focused on whether minimum resale price maintenance met the Court's current test for *per se* prohibitions – that is, whether the restraint always or almost always tends to restrict competition and decrease output. The Court began by concluding that the reasons originally offered in *Dr. Miles* for *per se* treatment were no longer valid. Next, the Court concluded that there were at least two possible procompetitive justifications for allowing companies to set a minimum resale price. First, a minimum price can help ensure that retailers provide services that enhance interbrand competition. Second, a minimum price may enable new companies and brands to enter the market. Given these potential procompetitive effects, the Court concluded that *per se* treatment was inappropriate.

"The impact of *Leegin* remains unclear. The Court offered little guidance to trial courts in applying the rule of reason in future cases. The Court did suggest that courts should scrutinize restraints more carefully if they are adopted by many manufacturers in the same market or if they are adopted at the behest of retailers; that such restraints are not likely to have anticompetitive effects unless the manufacturer (or the retailer) has market power; and that lower courts could 'devise rules over time for offering proof, or even presumptions where justified, to make the rule of reason a fair and efficient way to prohibit anticompetitive restraints and to promote procompetitive ones.' Companies should anticipate a period of adjustment as trial courts begin to apply *Leegin*. Although plaintiffs may face a higher burden under the rule of reason, that burden may be met in an appropriate case, and the consequences of violating the antitrust laws remain severe, including treble damages and attorneys fees."<sup>1</sup>

As Middleton and others also note, state laws can also restrict minimum resale price agreements. It is yet to be seen whether these states follow the tone of *Leegin* by loosening these laws, or potentially respond in the opposite direction by strengthening the state restrictions on these arrangements. Publishers that seek to develop resale price maintenance programs would be wise to seek counsel regarding each state's laws that apply to the program, as well as an assessment of how federal courts interpret and apply

*Leegin* over the coming months and years.

Will the ability to sign agreements that maintain resale pricing significantly reduce the discounting of books? Under the new flexibility of the rule of reason, will publishers pursue retail price maintenance programs to encourage the sale of their products by full-service retailers that carry their backlist and know their products, with a related damper on the growth of book sales by Internet retailers? Or, will *Leegin* not have any significant impact at all, in light of the fact that publishers and other manufacturers have for years been free to unilaterally stop selling to retailers that do not follow suggested minimum pricing policies, and have chosen in large part not to pursue such programs? This last result may be the most likely for most types of book products, but for now these are open questions.

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Brian Flagler founded Flagler Law Group in spring 2006, where his practice focuses on publishers, designers, producers, and distributors of Christian media. Before founding the firm, Mr. Flagler served as Vice President of Administration & General Counsel of Multnomah Publishers, Inc., where he led the human resources, information technology, operations, and legal departments and was responsible for all corporate legal matters for the company. Mr. Flagler also served as a member of Multnomah's executive leadership committee. Previously, Mr. Flagler practiced intellectual property and corporate law in the Portland, Oregon office of Davis Wright Tremaine LLP, a leading international media firm. Prior to moving to the west coast, Mr. Flagler practiced with Troutman Sanders LLP in Atlanta, Georgia and served as adjunct instructor of intellectual property law at Clayton College & State University. Mr. Flagler holds a Juris Doctor from the University of Virginia School of Law.

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