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I. INTRODUCTION

The 2007 U.S. Supreme Court decision in *Leegin*[2] set in motion a landslide by overturning a 96-year old precedent. After identifying that the probability of anticompetitive resale price maintenance ("RPM") was too low to justify a *per se* prohibition, the Court now advocated a rule of reason approach to RPM cases. Despite the following protracted debate regarding the interface between economic theory and legal rules, the landscape for RPM remains blurred across jurisdictions.

RPM, often referred to as vertical price-fixing, occurs when suppliers fix the (minimum) price at which distributors can resell its products. While the U.S. federal analysis took a dramatic U-turn to review RPM under the rule of reason, the European approach remains largely unchanged. RPM is classified as a restriction of competition by object that will be presumed to breach Article 101(1) of the Treaty on the Functioning of the European Union and, consequently, presumed not to contain the sufficient efficiency requirements of Article 101(3).

This harsh stance does not fully embrace an economics-based approach as it fails to truly recognize that market power is a prerequisite for consumer harm to occur. Consequently, the European Commission's ("EC") hostile approach causes the risk of over-enforcement through "type 1" errors where pro-competitive restraints are prohibited. This creates the risk that undertakings will not engage in pro-competitive RPM and will, instead, implement other vertical restraints that have a lower likelihood of providing welfare benefits to consumers.

II. THE UNITED STATES AND EUROPE ARE NOT READING FROM THE SAME PAGE

In *Leegin*, a manufacturer of ladies' shoes, handbags, and other leather accessories adopted an RPM scheme for its "Brighton" product line. This scheme was implemented through Leegin's policy of refusing to sell to retailers that discounted its products below the suggested retail prices. However, PSKS (the parent of retailer Kay's Kloset) offered discounts and had its contract terminated. Consequently, PSKS brought an action claiming that Leegin's policy of setting minimum retail prices amounted to a *per se* infringement of antitrust rules.

The Supreme Court, by a majority of 5-4, finally overturned the *per se* rule by determining that RPM should be assessed using the rule of reason. This means that federal courts must balance the pro-competitive efficiency benefits of RPM against the potential anticompetitive harm before finding that an infringement has occurred. The Supreme Court

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[2] Leegin Creative Leather Products, Inc. v. PSKS, Inc., (127 S. Ct. 2705 (2007)).

identified a number of anticompetitive effects of RPM, such as facilitating collusion of a manufacturer or retailer cartel and/or allowing a manufacturer with significant market power to incentivize retailers not to sell products to smaller rivals or new entrants. Additionally, Justice Kennedy, who wrote for the majority, also identified an important qualification to the anticompetitive harm, in that a lack of market power reduces the risk of anticompetitive harm. This qualification ensures the application of a fully economic approach and that "type 1" errors are avoided.

While economists had already identified the pro-competitive benefits of RPM long before *Leegin*, the case marks an important turning point with the majority finding that RPM is "more likely to be used to enhance efficiency than for anticompetitive purposes." Notably, however, the Supreme Court fails to back up this assertion by showing precisely why the pro-competitive benefits of RPM are more likely to occur than the harmful ones. Another shortcoming of the case is the absence of a structured approach, as the judgment lacks any guidance on how a rule of reason approach to RPM should be applied in practice.

Several years on, *Leegin* continues to be controversial. This is not only because it overturned an almost century-old precedent, but also because there remains vocal dissent in the United States against the rule of reason approach and the landscape at the individual U.S. state level remains uncertain.[3] The long-term effect of *Leegin*, therefore, lacks clarity in relation to state antitrust laws.

III. *LEEGIN*—THE REACTION AND INACTION

The *Leegin* case is also controversial as it sparked a widespread call for the object classification of RPM to be overhauled at the European level when the EC embarked on an update of its Vertical Block Exemption ("VBER") in the summer of 2009. Several commentators advocated that the EC should move towards a more refined economics-based approach.

One of the most effective suggestions was based on incorporating the concept of market power into the assessment of RPM. It is widely recognized that market power is required for consumer harm flowing from a vertical restraint to occur. For this reason, the Economic Advisory Group on Competition Policy ("EAGCP") suggested that the *de minimis* notice should be amended to ensure that firms with less than 30 percent market share fall outside Article 101(1) as they lack the requisite market power to cause consumer harm.[4] This would ensure that collusion between upstream manufacturers as well as downstream retailers is prevented, without risking over-enforcement of RPM on entities with market shares that are too small to be detrimental to consumer welfare.

Additionally, EAGCP also pointed out that the former Article 8 (and current Article 6) of the VBER already adequately safeguarded against any industry-wide collusion that may soften competition through interlocking relationships with two or more suppliers selling its products to two or more retailers. Such collusive effects are captured under Article 6 of the VBER, which

[3] For example, Maryland specifically enacted a statute in 2009 repealing the rule of reason approach to RPM.

[4] *Hardcore restrictions under the Block Exemption Regulation on vertical agreements: An economic view,* Vertical Restraints subgroup (September 2009).

allows the exemption to be revoked in situations of networks of vertical restraints covering more than 50 percent of the market.

Thus, the simple change of the *de minimis* threshold, together with Article 6, would refine the enforcement policy to ensure that only undertakings with market power, and therefore the ability to appreciably harm consumers, are captured under Article 101(1).

Another suggestion was put forward by Reindl to develop a more "sensible analytical approach" by moving RPM out of Article 4 as a hardcore restriction and into Article 5 for non-exempted restraints.[5] This more reasonable approach would result in RPM not benefiting from the safe harbor of the VBER but, at the same time, not categorizing it as a hardcore restriction. The practical implications of removing its hardcore classification would be that RPM would be analyzed in its market context, and it would also negate the presumption that RPM would not satisfy Article 101(3). This amendment would enable a more economics-based analysis on a case-by-case basis.

Bennett *et al.* also put forward a "more nuanced" approach that attempted to ensure that any presumption of illegality under Article 101(1) could truly be rebutted.[6] This would be achieved through a tripartite approach to weed out harmless RPM by using three "screens." The failure of one of the conditions described below would be required for there to be a credible theory of harm associated with the RPM:

1. that there be no unilateral market power upstream;
2. that there be no significant buyer power downstream; and
3. that there be assurance that the RPM is not applied by firms that cumulatively account for a significant share of the upstream market.

Unfortunately, in comparison to the more workable suggestions proposed by the EAGCP and Reindl, these screens in practice lack the clear-cut methodology that would give undertakings the legal certainty that they require when implementing pro-competitive RPM.

While the EC did not agree with any of the suggestions to amend the analysis of RPM, it did agree with Bennett *et al.*'s conclusion that there lacks sufficient evidence to justify moving RPM from the object box into the effect box. The EC therefore maintained the hardcore classification of RPM in the updated VBER as, on the balance of probabilities, it considered that RPM very often leads to negative effects in the market.

The EC also recently commented that, when consulting on the updated VBER, discussions with the European Competition Network pointed to the pertinence of a cautious approach in cases which were mainly handled by National Competition Authorities. This conclusion was supposedly due to the fact that, in general, undertakings had been unsuccessful in

[5] Andreas P. Reindl, *Resale Price Maintenance and Article 101: Developing a More Sensible Analytical Approach*, 33 FORDHAM INT'L L.J. 1300 (2011).

[6] *Resale price maintenance: Explaining the controversy, and small step towards a more nuanced policy*, Matthew Bennett, Amelia Fletcher, Emanuele Giovannetti, & David Stallibrass, Office of Fair Trading, MPRA paper 21121 (30 January 2010).

their attempts to justify RPM through efficiencies.[7] However, this argument is circular. What the EC fails to recognize is that the paucity of successful efficiency cases is largely due to the framework and dual presumptions that flow from RPM being a hardcore restriction—the presumption of illegality in Article 101(1) and the presumption that efficiencies are unlikely in Article 101(3).

IV. THE VERTICAL GUIDELINES AND THE SEVEN DEADLY SINS

By maintaining RPM as a hardcore restriction of competition, the updated VBER and Vertical Guidelines that came into force on June 1, 2010 represent a missed opportunity to align enforcement policy with economic theory. The Vertical Guidelines identify seven theories of harm resulting from RPM. Each of these are dealt with in turn:

1. **Facilitating collusion between suppliers:** Enhancing price transparency on the market enables suppliers to monitor when other suppliers cut their prices, thus facilitating cartel behavior.
2. **Facilitating collusion between retailers:** RPM may also facilitate collusion between retailers at the distribution level by eliminating interbrand competition.
3. **Softening competition:** This occurs through the existence of interlocking relationships involving suppliers who use the same retailers to distribute their products where the market is saturated by others also using RPM.
4. **Price increase:** The immediate effect of RPM is to increase prices.
5. **Commitment problem:** A supplier with significant market power that implements RPM can commit itself not to lower the wholesale price charged to new retailers in order to increase its market share.
6. **Foreclosure of competing suppliers:** A supplier with some degree of market power may impose RPM to foreclose access to rival brands.
7. **Foreclosure of innovative retailers:** RPM can cause barriers to entry against innovative dealers.

In essence, there is a large degree of overlap between these theories of harm that can be boiled down to three risks: (i) collusion between manufacturers/retailers, (ii) foreclosure by a dominant supplier or a supplier with market power, and (iii) softening of competition through widespread use of RPM in a given market.

In the updated guidelines, the EC demonstrated some movement towards recognizing efficiencies. Nonetheless, the efficiencies identified in the Vertical Guidelines have limited and only temporary applications—specifically where there is a launch of a new product, a short-term low price campaign in a franchise system, or a program to eliminate free-riding of retailers on the provision of additional pre-sale services by other retailers of complex goods.

Thus, while seemingly attempting to be more receptive to RPM, the EC does not fully embrace the economic arguments on the pro-competitive aspects of RPM which Bennett *et al.*

[7] *Roundtable on vertical restraints for on-line sales*, OECD DAF/COMP(2013)13, p. 80 (12 September 2013).

point out are "older and more established than that on its anticompetitive effects." Clearly there remains a misalignment between economic theory and enforcement policy as economists regard RPM as "a vertical restraint that happens to involve price restrictions, not a price constraint that deserves automatically to be placed in the same category as horizontal pricing agreements."[8] The hostile approach to RPM in the Vertical Guidelines is still far from being fully economics-based.

Unfortunately, there have been no recent EC decisions involving RPM to test this approach. There have, however, been interesting developments from the National Competition Authorities.

V. RECENT CASES/ANOMALIES—TRYING TO CONNECT THE DOTS

The latest cases on RPM have been policed at a national level, which sometimes deviate from the EC's position. Following *Leegin*, the CNC, the competition authority in Spain, was firmly on the side of an economic- and effects-based framework when analyzing RPM.[9] Since then, Spain has on two occasions applied a *de minimis* threshold and decided that the market shares of the undertakings concerned were too low to have an anticompetitive effect on competition.[10] For example, in *El Corral de las Flamencas*, the CNC considered, based on the legal and economic context, that this conduct did not significantly affect competition as El Corral's market share was less than 1 percent. It is too early to reach any conclusions on whether Spain is turning towards an effects-based analysis or whether these two cases are simply anomalies.

The OFT has also taken an interesting approach to RPM in the United Kingdom. At the time of writing, the OFT is investigating two RPM cases which it has, from the public perspective at least, dealt with in different ways. The first investigation relates to InterContinental Hotels Group's prohibition on online travel agencies Booking.com and Expedia from discounting hotels' room-only prices. The OFT makes no public mention that this practice constitutes RPM which, put in context of the OFT provisionally recognizing the existence of potential efficiencies beyond those identified in the Vertical Guidelines, marks an unusual RPM case.

The second OFT investigation alleges that DB Apparel engaged in RPM with John Lewis, Debenhams and House of Fraser. Contrary to the hotel investigation, the OFT has taken a more forthright approach by explicitly identifying RPM and remarking that "The OFT takes allegations of price fixing seriously."[11]

While some Spanish and U.K. examples suggest a more flexible approach, it is too soon to put these into focus and see the full implications on the enforcement policy of the two competition authorities.

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[8] Derek Ridyard, *Resale Price Maintenance: An overview of EU and national case law*, e-Competitions, No.41915 (24 January 2012).

[9] *Roundtable on resale price maintenance*, OECD DAF/COMP(2008)37, p. 187 (10 September 2009).

[10] *See* decision of 3 December 2009 in case 0105/08, El Corral de las Flamencas, and decision of 17 December 2010 in case S/0257/10, Natura Bissé Internacional.

[11] *See* http://www.oft.gov.uk/news-and-updates/press/2013/64-13.

VI. CONCLUSION

The boundaries to RPM at the state levels in the United States and in Europe (or at least in the United Kingdom and Spain) remain blurred. Additionally, despite the active landscape of cases in China, uncertainties still persist on whether a rule of reason or *per se* approach applies.

Back in Europe, the EC's enforcement policy has been to defer to National Competition Authorities, so it may still be some time before we can see the practical implications of the theoretical recognition of efficiencies in the VBER. While it is too soon to tell where these National Competition Authorities are moving towards a more nuanced approach, it is clear that the hardcore classification of RPM and presumption of illegality that follows give rise to a high-risk of over-enforcement.