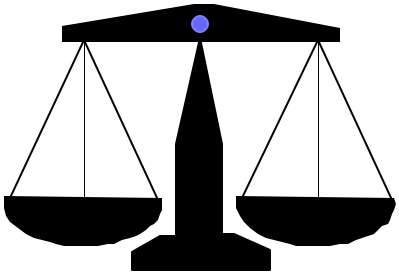

GENERAL COUNSEL CORNER

By Peter H. Gunst, Esquire

The Small Businessman and the New Supreme Court

For as long as I can remember, courts, scholars and politicians have lauded the independence and entrepreneurship of small business people such as service station dealers.

A cornerstone of that independence and entrepreneurship was the dealer's right to set the prices at which his or her goods were offered to the public.

After all, it was the dealer who had to make payroll and ran the risk of economic loss. Why shouldn't he or she be entitled to control his or her retail prices?

The dealer's right to control his or her price appeared set in stone. Almost one hundred years ago, in its landmark 1911 decision, *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, the United States Supreme Court had held emphatically that it was *per se* illegal under the Sherman Act for a manufacturer to prohibit a dealer from discounting the goods that he or she purchased from a manufacturer and resold to the public.

Congress apparently agreed with the Supreme Court's decision. Not only did it take no action to disapprove of the *Dr. Miles* decision, but in 1975 it repealed the Miller-Tydings Fair Trade Act, which had permitted individual states to enact "fair trade" laws authorizing minimum resale price maintenance. The result of Congress' repeal was to enforce uniformly across the nation the Sherman Act's ban on resale price maintenance.

Further, Congress later forbade the Department of Justice and the Federal Trade Commission from using any funds to oppose the *Dr. Miles* doctrine.

The Department of Justice and the Federal Trade Commission at first agreed with the wisdom of protecting dealers from manufacturer interference with their pricing discretion.

About the time that the Miller-Tydings Fair Trade Act was repealed, the Department of Justice advised Congress that resale price maintenance had resulted in raising prices paid by consumers by from 19% to 27%. The Federal Trade Commission staff later agreed that its studies indicated that resale price maintenance "in most cases increased the prices of products" sold to the public. In sum, *Dr. Miles* was good for consumers as well as dealers.

A large majority of states also saw the wisdom of the *Dr. Miles* rule. When the Supreme Court recently accepted an appeal challenging the continued viability of the decision, the attorneys general of thirty-seven states joined in urging that the Supreme Court not disturb the long-standing ban against resale price maintenance.

But enter the new majority on the United States Supreme Court. On June

28, 2007, by a 5-to-4 decision in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, that new majority jettisoned the *Dr. Miles* rule and held, henceforth, that resale price maintenance would be subject merely to "rule of reason" analysis, meaning that it would be prohibited only if a court found it to have a specific anticompetitive effect in a specific product and geographic market.

In the real world this means that resale price maintenance would go from being *per se* illegal to being - virtually - *per se* legal. In the real world, the cost and complexity of establishing a rule of reason violation, which entails presenting detailed expert and economic evidence, means that few if any plaintiffs could dare hope for success in the courts. In sum, the new majority gave manufacturers carte blanche to usurp dealer pricing discretion.

In a powerful dissent, Justice Breyer, most probably the leading antitrust expert on the Supreme Court, cogently argued against the new majority's determination, emphasizing the negative effect that overruling *Dr. Miles* would have both on intra-brand competition among dealers and inter-brand competition among manufacturers.

With respect to intra-brand competition, Justice Breyer emphasized that, by employing resale price maintenance, manufacturers "can prevent dealers from offering customers the lower prices that many customers prefer; they can prevent dealers from responding to changes in demand …; … they can inhibit expansion by more efficient dealers whose lower prices might otherwise attract more customers, stifling the development of new, more efficient modes of retailing; and so forth."

With respect to inter-brand competition, Judge Breyer observed that retail price maintenance arrangements "can help to reinforce competition-inhibiting behavior in firms in concentrated industries" by allowing them to police the marketplace against discounting practices that would lower prices to consumers.

Justice Breyer recognized that hypothetical arguments have been raised about presumed benefits that might result from scrapping *Dr. Miles' per se* prohibition. Thus, some manufacturers and economists have contended that ending the ban on retail price maintenance could prevent some dealers from taking a "free ride" on the efforts of others by discounting the price of products whose name and reputation had been built by the work of others.

But this mere hypothetical possibility was not dispositive, in Justice Breyer's mind or that of the three other justices who joined in his dissent.

To them, as Justice Breyer wrote, "the ultimate question is not whether but *how much*, 'free riding' of this sort takes place" and whether courts can easily identify instances in which the benefits of resale price maintenance are likely to outweigh potential harm.

Rejecting the majority's reliance on rule of reason analysis to resolve such issues, Justice Breyer concluded that, to the extent that rule of reason challenges were brought at all, they would involve "lengthy time-consuming argument among competing experts, as they seek to

apply abstract, highly technical, criteria to often ill-defined markets." In sum, the merely hypothetical arguments raised to justify retail price maintenance could not justify the almost total emasculation of the law imposed by the new majority.

Finally, and perhaps most significantly, Justice Breyer protested against the new majority's seemingly cavalier rejection of a long-standing precedent. Economic concentration both among manufacturers and dealers has increased over the past decades, rendering resale price maintenance even *more* dangerous to the public than it was when *Dr. Miles* was decided. Hence, the case for a *per se* rule appeared *stronger* than it was when *Dr. Miles* was decided.

Justice Breyer observed the relevant factors previously utilized by the Court in determining whether or not to overrule earlier precedent pointed almost uniformly to upholding the *Dr. Miles* decision. The case before the Court involved a statutory interpretation of which Congress had long approved; it did not create an "unworkable legal regime"; and it had long been relied upon as settled law.

As Justice Breyer concluded:

> The only safe predictions to make about today's decision is that it will likely raise the price of goods at retail and that it will create considerable legal turbulence as lower courts seek to develop workable principals.

So where do we go from here? For one thing, Congress could address the situation by clarifying the scope of the Sherman Act. Unfortunately, Congress in recent years has shown little willingness to side with small business persons against large manufacturers and their armies of lobbyists.

Alternatively, dealers could look to state antitrust regulation for protection. Most state antitrust laws, however, state an intention to be guided by the federal court's interpretation of federal antitrust law. So, here too, prospects are not sanguine.

Despite these obstacles, there is reason to believe that corrective action can be taken. After all, at least thirty-seven state attorney generals disagreed with the Court's conclusion, and there was a very strong four-justice dissent. Maybe, this time, corrective action will be taken to prevent dealer disenfranchisement and to protect consumers against artificial pricing levels imposed by manufacturers.

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