The Price Point

Newsletter of the ABA Section of Antitrust Law Pricing Conduct Committee

Volume 11, Issue 1 **Winter 2012**

We are pleased to bring you this issue of Pricing Conduct Committee's newsletter, which includes articles on pleading standards and minimum advertized pricing programs, as well as summaries of the first two programs in the Pricing Conduct Committee's Pricing Fundamentals Series.

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New & Noteworthy

New York v. Tempur-Pedic Int., Inc. (N.Y. Sup. Ct. App. Div., Jan. 30, 2012). It's not over yet... The State of New York has appealed the NY Supreme Court's dismissal of its petition seeking summary relief enjoining Tempur-Pedic from engaging in conduct allegedly in violation of NY General Business Law § 369-a. The NY Supreme Court rested its decision on three grounds, finding that (1) while § 369-a renders RPM contracts unenforceable, it does not make them illegal; (2) Tempur-Pedic's price restraints were contained in a unilateral policy, not in contracts to which retailers agreed to adhere; and (3) there was no evidence showing that Tempur-Pedic misled retailers into believing they were bound by an enforceable contract to set retail prices. On appeal, the OAG argues that (i) violating § 369-is illegal; (ii) as a matter of New York contract law, Tempur-Pedic violated § 369-a by banning discounting; and (iii) dismissal was improper given the Attorney General's allegations. Stay tuned.

Dayton Sup. Corp., v. Spa Steel Prod., Inc. (NDNY, Jan 13, 2012). Plaintiff Dayton Superior filed a breach-of-contract action to recover payments allegedly owed Plaintiff for goods that it had sold and delivered to Defendant Spa Steel. Spa Steel counterclaimed, alleging Plaintiff violated the Robinson-Patman Act's prohibition on discriminatory pricing among competing buyers of the same goods. On January 13, 2012, the District Court denied Plaintiff's motion to dismiss Defendant's counterclaim on the basis of failure to state a claim for price discrimination and a lack of standing, finding that Defendant plausibly pled a sufficient nexus for causation purposes between Plaintiff's allegedly discriminatory pricing and Defendant's alleged injury to withstand a motion to dismiss. In support of its counterclaim, Defendant submitted a customer's affidavit stating that such customer routinely bought from Defendant's competitors because they consistently offered the same products at prices 10% to 15% lower than Defendant. The Court found these allegations sufficient to show reasonably contemporaneous discriminatory sales of goods of like grade and quality, and an unlawful harm to competition resulting from the alleged price discrimination. The Court noted that whether Defendant's economic loss may ultimately be fairly attributed to Plaintiff's allegedly discriminatory-pricing practices is better reserved for a motion for summary judgment, should such a motion prove to be appropriate following discovery.

Call for Articles. The Price Point is seeking submissions for the Spring 2012 issue. Consistent with the Pricing Conduct Committee's focus, articles on resale price maintenance, predatory pricing, bundled pricing, price squeezes, or other pricing-related topics are welcome, as of course are articles on price discrimination and Robinson-Patman Act issues. Articles should be approximately 2,000 words in length, excluding notes. Submissions are due by April 15, 2012.

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Recent Price Discrimination Cases and "Plausible" Pleadings under *Twombly* and *Iqbal*

By: Mark M. Lawson & Devin C. Dolive

Recent case law highlights obstacles that the Supreme Court's "plausibility" pleading standard may pose to Robinson Patman Act plaintiffs and, in some cases, defendants. Because pricing and cost information is often in the exclusive control of RPA defendants, application of this "plausibility" standard at the motion-to-dismiss stage can deny RPA plaintiffs the very discovery that they would need in order to identify the facts that make their claims "plausible."

By way of background, in *Bell Atlantic Corp. v. Twombly*,[1] the Supreme Court rejected the well-known holding of *Conley v. Gibson*[2] that "a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief."[3] Rather, the *Twombly* Court held that, to survive a motion to dismiss, a plaintiff must allege "enough facts to state a claim to relief that is plausible on its face."[4] The Court stated:

> [A] plaintiff's obligation to provide the grounds of his entitlement to relief requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do. Factual allegations must be enough to raise a right to relief above the speculative level . . . .[5]

Subsequently, in *Ashcroft v. Iqbal,*[6] the Supreme Court provided additional guidance and held that the *Twombly* plausibility standard applied in all civil cases in federal courts.[7] The Court also set forth a two-pronged approach for federal courts to use when ruling on motions to dismiss. First, a court should distinguish between legal "conclusions" and actual "facts" pled in a complaint. Mere "conclusions" are "not entitled to the assumption of truth."[8] The Court explained: "While legal conclusions can provide the framework of a complaint, they must be supported by factual assumptions,"[9] and "[t]hreadbare recitals of the elements of a cause of action, supported by mere conclusory statements, do not suffice."[10] Second, even when well-pleaded factual allegations are present in the complaint, "a court should . . . then determine whether they plausibly give rise to an entitlement to relief."[11] The Supreme Court explained this concept of "plausibility" as follows:

> A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged. The plausibility standard is not akin to a "probability requirement," but it asks for more than a sheer possibility that a defendant has acted unlawfully. Where a complaint pleads facts that are "merely consistent with" a defendant's liability, it "stops short of the line between possibility and plausibility of 'entitlement to relief.'"[12]

As might be imagined, these requirements -- that a plaintiff plead "facts," as distinguished from "conclusions," and that these "facts," as pled, must make a claim "plausible" -- can pose a sometimes insurmountable burden on RPA plaintiffs. This is particularly true in the case of RPA plaintiffs who do not have pre-suit access to detailed information regarding a defendant's pricing and costs.

In *New Albany Tractor, Inc. v. Louisville Tractor, Inc.*,[13] for example, the Sixth Circuit affirmed the dismissal of a complaint under *Twombly* and *Iqbal* and held that RPA plaintiffs had failed to adequately plead their claims. There, the plaintiff, an equipment retailer (New Albany Tractor), had filed suit alleging that the defendants, a manufacturer of mowing equipment (Scag) and an exclusive wholesale distributor of the manufacturer's products (Louisville Tractor), had engaged in a discriminatory pricing scheme to reduce competition. The manufacturer defendant required the plaintiff retailer to purchase motors and parts from the wholesale distributor defendant. The manufacturer refused to sell directly to the plaintiff or to allow the plaintiff to purchase equipment from a different distributor.

Prior to the appeal, the district court had originally denied the defendants' motion to dismiss, after misinterpreting documentary evidence and

concluding that the manufacturer defendant had set the defendant distributor's prices.[14] The court then reconsidered its earlier decision, after the plaintiff admitted that the wholesale distributor defendant set its own prices and that the manufacturer defendant simply monitored the prices set by the exclusive distributor and exercised "some influence" over prices that it disliked. The district court held: "Plaintiff's allegation that Scag monitors Louisville Tractor's prices is insufficient. There must be some allegations that Scag 'set or controlled resale price.'"[15]

The Sixth Circuit affirmed, stating: "We agree that these cases [*Twombly* and *Iqbal*] require the District Court to dismiss the complaint with prejudice."[16] The Sixth Circuit further noted:

> [This new "plausibility" pleading standard causes a considerable problem for plaintiff here because defendants Scag and Louisville Tractor are apparently the only entities with the information about the price at which Scag sells its equipment to Louisville Tractor. This pricing information is necessary in order for New Albany to allege that it pays a discriminatory price for the same Scag equipment, as required by the language of the Act. This type of exclusive distribution structure makes it particularly difficult to determine whether discriminatory pricing exists.[17]

The Sixth Circuit also noted that, prior to *Twombly* and *Iqbal*, the RPA claim would in all likelihood have been allowed to proceed so that the plaintiff could conduct discovery:

> Before *Twombly* and *Iqbal*, courts would probably have allowed this case to proceed so that plaintiff could conduct discovery in order to gather the pricing information that is solely retained within the accounting system of Scag and Louisville Tractor. . . . In this case that [the *Twombly* standard] means . . . that plaintiff must allege specific facts of price discrimination even if those facts are only within the head or hands of the defendants. The plaintiff may not use the discovery process to obtain these facts after filing suit. The language of *Iqbal*, "not entitled to discovery," is binding on the lower federal courts.[18]

Another recent decision, *Coalition For A Level Playing Field, L.L.C. v. AutoZone, Inc.*,[19] also demonstrates the burden that *Twombly* and *Iqbal* impose on RPA plaintiffs. In *Coalition*, the federal district court concluded that a RPA complaint failed to state a claim from which relief can be granted because the complaint failed to "plausibly allege: (i) that disparate prices charged by defendants reflect anticompetitive price discrimination rather than permissible functional discounts; (ii) that those prices are not the product of materially different contractual arrangements; or (iii) that certain alleged discount arrangements are not merely non-price terms of sale (which do not implicate the [RPA])."[20]

The court in *Coalition* concluded the plaintiffs had failed to make allegations refuting the legality of functional discounts.[21] The court specifically explained why the complaint's allegations concerning discounts to plaintiffs' competitors were implausible under *Twombly* and *Iqbal*:

> [T]he complaint asks the Court to infer *illegal* price discrimination from the mere fact that there are differences in the prices charged to the retailer defendants, WDs, and jobbers. While this analytic move (in essence, and assumption that primary behavior that *could* be illegal *is*) was permissible and even encouraged under *Conley v. Gibson*, it is precisely the inference that *Twombly* and *Iqbal* caution against drawing in the absence of factual allegations demonstrating a plausible entitlement to relief.[22]

The district court also examined allegations of materially different contract terms at issue and concluded that the plaintiffs had failed to make necessary allegations addressing same:

> The complaint, however, ignores the possibility that these contract differences account for the lower prices paid by the retailer defendants, save for conclusory allegations that different provisions in the supply agreements entered

into by WDs, jobbers, and the retailer defendants are *really* disguised price terms. Absent a more particularized factual basis for drawing this broad-ranging legal conclusion, the allegations in the complaint are insufficient to state a § 2(a) claim.

> Finally, a number of the contract provisions challenged in the complaint relate to non-price terms of sale. Paragraph 90(G), for example alleges that the retailer defendants' vendor agreements "permit[ ] deferred payments on goods sold to defendants . . ." To be sure, this paragraph goes on to allege that deferred payments are "beyond and unrelated to credit terms awarded on the basis of defendants' or any other purchasers' credit rating, which amounts to the placement of interest-free capital with defendants by the manufacturers." But under *Twombly* and *Iqbal*, this allegation, which simply attempts to paraphrase the relevant legal test, is not enough. In view of the general rule that non-price terms are not regulated by § 2(a), *Corn Prods.*, 324 U.S. at 740, 65 S.Ct. 961, a more specific statement is necessary to support a plausible inference that non-price discrimination is, in fact, price discrimination.[23]

As to the plaintiffs' allegations regarding discriminatory advertising and promotional programs available to their competitors, the court found that plaintiffs had not met their pleading burden here either:

> Plaintiffs en masse assert against all defendants that "[e]very paragraph in the vendor agreement has financial implications and the whole package is an advertising and promotional program for the distribution of the manufacturer's designated products through the retailer's distribution system," and the plaintiffs were not offered similar opportunities. . . . While it is possible that at some point one among hundreds of plaintiffs was denied a promotional opportunity, no one plaintiff has alleged a plausible claim, much less all of them individually. . . . Rule 8 requires "a short and plan statement of the claim *showing* that the pleader is entitled to relief," not conclusory allegations that defendants violate the law.[24]

The court in *Coalition* granted the plaintiffs leave to amend their complaint to attempt to remedy their omissions.[25] However, this was of little help to the plaintiffs. In their proposed amended complaint, the plaintiffs focused on price discrimination not with the respect to auto parts,[26] but with respect to auto part product lines, asserting that the total costs of the parts at issue could not be determined without discovery. The proposed complaint also added allegations that explicitly disclaimed the possibility that any price differentials were due to lawful conduct such as functional discounts or different terms of sale.[27] The court concluded that the proposed complaint nonetheless failed to state a claim for price discrimination:

> [M]ost of those factual allegations are either conclusory or non-responsive to the existence of price discrimination. . . . [T]he relative success of the retailer defendants in the auto parts market as compared to the dwindling small retailer plaintiffs is as easily explained by numerous other competitive differences without concluding that defendants routinely violate the RPA. . . . [S]imilarly, the fact that the retailer plaintiffs themselves charge higher retail prices than the retailer defendants, is also as easily explained by their competitive differences than by the alleged discriminatory pricing at a different level of distribution. . . . [T]he allegation that the retailer defendants intentionally hide their price discrimination is itself conclusory and depends on the existence of that price discrimination; absent facts tending to show that the various manufacturer and retailer

> defendants are engaged in a coverup, that allegation does not support the related allegation of wrongdoing.[28]

The court also concluded that the plaintiffs failed to provide in their proposed complaint any plausible allegations regarding advertising and promotional programs: "The Proposed Complaint again provides no description as to which of the nine defendants discriminated with respect to which programs, nor does it describe which particular plaintiffs were denied promotional opportunities or were injured thereby."[29] The Court also answered "Plaintiffs' implicit plea for discovery":

> Plaintiffs essentially concede that they cannot plead factual content supporting their claims because the requisite pricing information is unavailable to them -- it is in the hands of defendants. . . .
>
> * * *
>
> Plaintiffs' implicit plea for discovery runs contrary to the pleading requirements of *Iqbal* and *Twombly*.[30]

On the other hand, *Twombly* and *Iqbal* do not necessarily pose an insurmountable burden in terms of pleading competitive injury.[31] For example, in *Dayton Superior Corp. v. Marjam Supply Co.,*[32] the court concluded that the plaintiff had in fact properly plead the causation element of antitrust injury, stating:

> Marjam alleges that it competed with Barker and Spa to sell products, including the Product, "to the concrete contractor specialist and flooring specialist segments" in the relevant market during the time period at issue. Marjam further alleges that during this time period, Dayton sold the Product to Barker and Spa (the favored purchasers) "at an average sales price substantially less than Dayton charged to Marjam." As a result, both Spa and Barker were able to sell the Product to, for example, A Quest, but Marjam was not.
>
> . . . Marjam has pled that it suffered an injury to its business that "flow[ed]" from Dayton's alleged price discrimination.[33]

Interestingly, the defendant in this case tried to argue that the specific factual examples provided in the complaint were *de minimus*, but the court rejected this argument:

> Dayton argues that "the only head-to-head competition alleged - for a sale to A Quest Corp. - represents de minimis harm that does not suffice to demonstrate injury to competition . . . . " . . . Marjam's pleading makes clear that its allegations involving resales of the Product that it allegedly lost to Barker and Spa are pled "[b]y way of example only." Thus, the Court finds that Marjam has alleged enough facts at this point to proceed to discovery on the First Counterclaim.[34]

As such, it can be argued that, even under *Twombly* and *Iqbal*, a plaintiff is ***not*** required to plead the specifics of ***all*** instances of price discrimination or damages. For example, one court, in the context of a Sherman Act claim, noted: "*Twombly* does 'not require heightened fact pleadings of specifics, but only enough facts to state a claim to relief that is plausible on its face.' . . . Here, the MAC contains direct or inferential allegations respecting all material elements to sustain a recovery under the Sherman Act."[35]

Where does this leave us? First, *Twombly* and *Iqbal* obviously make the pleading of a RPA claim much more difficult for a plaintiff. Indeed, while the Supreme Court has previously noted that, "[i]n antitrust cases, where the 'proof is largely in the hands of the alleged conspirators,' dismissals prior to giving the plaintiff ample opportunity for discovery should be granted very sparingly,"[36] *Twombly* and *Iqbal* unequivocally reverse this proposition.[37]

Second, and while there does not appear to be any RPA case law on this point, *Twombly* and *Iqbal* arguably require the same "plausibility" pleading standard for affirmative defenses as for allegations in a complaint.[38] Thus, a defendant asserting affirmative defenses to a price discrimination claim arguably now has the burden of pleading those defenses in accord with the "plausibility" standard for pleading. For example, if a defendant asserts the meeting competition defense and claims that it offered a lower price to a competitor of the plaintiff to meet competition, the defendant may need to be prepared to state the

"who, where, or when" of the circumstances surrounding this offer.[39] Similarly, a defendant asserting the cost justification defense maybe required to submit facts including cost information establishing why they had a lower cost when they sold to one party versus another.

Third, even though courts are more likely under *Twombly* and *Iqbal* to look at price discrimination complaints with the critical eye to determine plausibility, courts nonetheless may remain free to grant leave to amend a defective pleading.

Fourth, *Twombly* and *Iqbal* only apply in federal court and in those states that have adopted the "plausibility" standard. While some state courts have adopted *Twombly* and *Iqbal*;[40] others have rejected this standard [41] and yet others have declined to decide the issue to date.[42]

Fifth, there are a plethora of state price discrimination statutes on the books, not all of which are direct "analogues" to the RPA.[43] Where the state statute is an "analogue" to the RPA, courts maybe likely to find that a dismissal of an RPA claim likewise is applicable to the state law claims.[44] However, given the uncertain scope of many of these statutes and the fact that some statutes were evidently drafted with discovery in mind,[45] a federal court, even when dismissing a federal RPA claim, may be inclined to simply remand or dismiss without prejudice any state law pricing claims.[46] At a minimum, in those states that have not adopted the *Twombly* and *Iqbal* pleading standards, one might expect potential RPA plaintiffs to begin filing more complaints in state court relying on state statutes, so as to avoid adjudication of their claims by a federal court bound to apply pre-discovery "plausibility" standards to the plaintiffs' pleadings. Alternatively, in those states that have adopted pre-suit discovery procedures more expansive those provided for in the federal rules,[47] a potential RPA plaintiff may be able to use state court procedures to obtain discovery of pricing and cost information without even filing a complaint.[48]

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[1] 550 U.S. 544 (2007).

[2] 355 U.S. 41, 45-46 (1957).

[3] 550 U.S. at 561 (quoting *Conley,* 355 U.S. at 45-46).

[4] 550 U.S. at 570.

[5] *Id.* at 555.

[6] 129 S. Ct. 1937 (2009).

[7] *Id.* at 1953.

[8] 129 S.Ct. at 1950.

[9] *Id.*

[10] *Id.* at 1949 (citing *Twombly*, 550 U.S. at 555).

[11] *Id.* at 1950.

[12] *Id.* at 1949 (quoting *Twombly*, 550 U.S. at 556-57).

[13] 650 F.3d 1046 (6th Cir. 2011).

[14] *New Albany Tractor, Inc. v. Louisville Tractor, Inc.,* Civil Action No. 3:08-CV-664-H, 2010 WL 59206 (W.D. Ky. Jan. 5, 2010).

[15] *Id.* at *1 (case citation omitted).

[16] 650 F.3d at 1048.

[17] *Id.* at 1050.

[18] *Id.* at 1051.

[19] 737 F. Supp. 2d 194 (S.D.N.Y. 2010).

[20] *Id.* at 208-09.

[21] *See id.* at 215-16.

[22] *Id.* at 210 (emphasis in original).

[23] *Id.* at 216-17.

[24] *Id.* at 218 (record citations omitted).

[25] *Id.* at 219.

[26] *Coalition For A Level Playing Field, L.L.C. v. AutoZone, Inc.*, No. 1:04-cv-08450-RJH, 2011 WL 4470742, at * 4 (S.D.N.Y. Sept. 28, 2011).

[27] *Id.* at *6.

[28] *Id.* at * 7-8 (record citations omitted).

[29] *Id.* at *6.

[30] *Id.* at *9-11.

[31] *But see G.L.M. Sec. & Sound, Inc. v. LoJack Corp.*, No. 10-CV-04701 (JS)(ARL), 2011 WL 4594825, at *14-15 (E.D.N.Y. Sept. 30, 2011) (finding plaintiff's complaint to be factually deficient in terms of pleading competitive injury).

[32] No. 07 CV 5215 (DRH)(WDW), 2011 WL 710450 (E.D.N.Y. Feb. 22, 2011).

[33] *Id.* at *8 (record citations omitted).

[34] *Id.* at *11 (record citations omitted).

[35] *In re Refrigerant Compressors Antitrust Litig.*, 795 F.Supp.2d 647, 661 (E.D. Mich. 2011); *but see In re Urethane Antitrust Litig.*, 663 F. Supp. 2d 1067, 1076 (D. Kan. 2009) (holding that the plaintiffs' allegations regarding the existence of a conspiracy were sufficient for one period of time but agreeing with the defendants that the plaintiffs had "failed to state a cause of action for antitrust liability under the *Twombly* standard for the period prior to 1999.").

[36] *Hospital Bldg. Co. v. Trustees of Rex Hospital,* 425 U.S. 738, 746 (1976) (quoting *Poller v. Columbia Broadcasting Sys. Inc.*, 368 U.S. 464, 473 (1962)).

[37] Even before *Twombly* and *Iqbal*, the Supreme Court's *Hospital Building* and *Poller* holdings had been routinely questioned, particularly at the summary judgment stage. *See, e.g., Emigra Group, LLC v. Fragomen, Del Rey, Bernsen & Loewy, LLP*, 612 F.Supp.2d 330, 344, n. 38 (S.D.N.Y. 2009) ("*Celotex, PepsiCo,* and *Tops Markets*, among other cases, effectively have overruled a large number of earlier cases that indicated that summary judgment was disfavored, especially in antitrust cases."); *Petruzzi's IGA Supermarkets, Inc. v. Darling-Delaware Co.*, No. 86-0386, 1992 WL 212230, at * 3 (M.D. Pa. July 31, 1992) ("Summary judgment was formerly regarded as an anathema in antitrust cases involving complex economic theories and issues. . . . That viewed changed with more recent Supreme Court decisions, . . . , which recognized the utility of summary judgment motions in such cases for sorting out complex issues and limiting the possibility that defendants against whom there is little or no evidence of wrongdoing will be compelled to expend large sums defending the claims brought against them."), *aff'd & rev'd in part on other grounds*, 998 F.2d 1224 (3d Cir. 1993).

[38] *See, e.g., Shinew v. Wszola,* No. 08-14256, 2009 WL 1076279, at *3 (E.D. Mich. Apr. 21, 2009) ("[T]he general rules of pleading . . . applicable to the statement of a claim also govern the statement of affirmative defenses under Federal Rule 8(c)."); *United States v. Quadrini,* No. 2:07-CV-13227, 2007 WL 4303213, at *3 (E.D. Mich. Dec. 6, 2007) (affirmative defense should be stricken under Rule 12(f) if it does not meet the pleading standards of Rule 8); *Hayne v. Green Ford Sales, Inc.*, 263 F.R.D. 647, 650 (D. Kan. 2009) (affirmative defenses must allege factual allegations sufficient to establish plausibility under Rule 8(b)(1)(A)); *Burget v. Capital West Securities, Inc.*, No. CIV-09-1015-M, 2009 WL 4807619, at *2 (W.D. Okla. Dec. 8, 2009) (adverse parties should be provided enough information about an affirmative defense to allow them to tailor their discovery); *Safeco Insurance Co. of America v. O'Hara Corp.*, No. 08-CV-10545, 2008 WL 2558015, at *1 (E.D. Mich. June 25, 2008). Other district courts have disagreed. *See, e.g., Dudley v. Regions Financial Corp.*, Civil Action No. 1:11-CV-2700-RLV, slip op. at 3 (N.D. Ga. Jan. 26, 2012) ("While some courts have broadly interpreted the impact and effect of these two cases, the U.S. Supreme Court did not, in either case, address the pleading standard applicable to a defendant's admissions, denials, or affirmative defenses under Rule 8(b) or (c). Therefore, this court concludes that these two cases are not relevant when evaluating affirmative defenses."); *Charleswell v. Chase Manhattan Bank, N.A.*, No. 01-119, 2009 WL 4981730, at *4 (D.V.I. Dec. 8, 2009) (in explaining why *Twombly* does not apply to affirmative defenses, the court noted that the text of F.R.C.P. 8(a)(2) requires the pleading of facts and is, distinct from Rule 8(c)(1)); *First National Ins. Co. of America v. Camps Services, Ltd.*, No. 08-cv-12805, 2009 WL 22861, at *2 (E.D. Mich. Jan. 5, 2009) (plausibility standard does not apply to affirmative defenses); *Kaufmann v. Prudential Ins. Co. of America,* No. 09-10239-RGS, 2009 WL 2449872, at *1 (D. Mass. Aug. 6, 2009) (noting that "sauce for the goose is sauce for the gander," but, due to the commonly recognized usage of the affirmative defenses listed in Rule 8(c)(1), these defenses intrinsically provide sufficient notice to satisfy the plausibility standard).

[39] *Twombly,* 550 U.S. at 565 n.10 (antitrust defendant is not provided sufficient notice of his role in the alleged conspiracy in which no "who, where, or when" allegations are included).

[40] *See, e.g., Doe v. Board of Regents of the University of Nebraska*, 788 N.W.2d. 264, 278 (Neb. 2010) ("[W]e believe that the Court's decision in *Twombly* provides a balanced approach for determining whether a complaint should survive a motion to dismiss and proceed to discovery."); *Iannacchino v. Ford Motor Co.*, 888 N.E.2d 879, 890 (Mass. 2008) ("[W]e take the opportunity to adopt the refinement of that standard that was recently articulated by the United States Supreme Court in *Bell Atl. Corp. v. Twombly,* 550 U.S. 544, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007).").

[41] *See, e.g., Webb v. Nashville Area Habitat For Humanity, Inc.*, 346 S.W.3d 422, 437 (Tenn. 2011) ("Our motion-to-dismiss jurisprudence reflects the principle that this stage of the proceedings is particularly ill-suited for an evaluation of the likelihood of success on the merits or of the weight of the facts pleaded, or as a docket-clearing mechanism. . . . We decline to reinterpret Rule 8 to require a pleader to demonstrate 'plausibility' and continue to adhere to the well established standards set forth in section 1 of this opinion."); *Crum v. Johns Manville, Inc.*, 19 So.3d 208, 212 n. 2 (Ala. Civ. App. 2009) ("Our supreme court has adopted the standard set forth in *Conley v. Gibson*, [355 U.S. 41, 78 S.Ct. 99, 2 L.Ed.2d 80 (1957)], for the dismissal of claims under Rule 12(b)(6), Ala. R. Civ. P. Until such time as our supreme court decides to alter or abrogate this standard, we are bound to apply it, the United States Supreme Court's decision in *Twombly,* supra, notwithstanding.").

[42] *See, e.g., Solers, Inc. v. Doe*, 977 A.2d 941, 948 n. 5 (D.C. App. 2009) ("This appeal does not require us to decide whether this court will follow the 'facial plausibility' standard recently discussed in Ashcroft v. Iqbal, --U.S.--, 129 S.Ct. 1937, 1949, 173 L.Ed.2d 868 (2009).").

[43] To give an example of one obvious difference between some state statutes and the RPA, not all state statutes require that there be "competitive injury" caused by price discrimination and instead may establish a *per se* rule. *See, e.g., Obstetrical & Gynecological Assocs. of Neenah, S.C. v. Landig*, 384 N.W.2d 719, 721 (Wis. App. 1986) ("The Wisconsin legislature apparently has enacted anti-trust laws containing a *per se* rule. . . . [S]ec. 218.01(9), Stats., dealing with auto dealerships, appear to have undergone *per se* treatment."); *see also* Bruce P. White, *Arizona's New Equipment Dealer Protection Laws*, 30-FEB ARIZONA ATT'Y 20-22 (Feb. 1994).

[44] *Cf. In re Plavix Indirect Purchaser Antitrust Litig.*, No. 1:06-cv-226, 2011 WL 335034, at *5 (S.D. Ohio, Jan. 31, 2011) ("Accordingly, since Plaintiffs fail to state a claim under the Sherman Act, and since the state antitrust claims are based on the same allegations, the state law claims are also dismissed."); *Rick-Mik Enterprises, Inc. v. Equilon Enterprises, LLC*, 532 F.3d 963, 976 n. 5 (9th Cir. 2008) ("The state law antitrust claims are derivative of the federal law claims. Because the federal claims fail, the state law claims fail.").

[45] For example, various state Motor Fuel Marketing Acts use an invoice-based definition of costs for the purpose of determining whether a sale is below cost. *See* ALA. CODE § 8-22-4(15); MO. STAT. § 416.605(2). Such invoices would not ordinarily be available to a plaintiff absent discovery.

[46] *See, e.g., Astra Media Group, LLC v. Clear Channel Taxi Media, LLC,* 414 Fed. Appx. 334, 337 (2d Cir. 2011) (affirming dismissal of § 2 Sherman Act predatory pricing and price discrimination claims, remanding state law claims and stating: "Here, it appears that Astra Media's remaining claims raise unsettled questions of state law. Perhaps most importantly, there is a question as to whether the New York courts have adopted - or would adopt - the *Iqbal* pleading standard, under which several of Astra Media's claims were dismissed by the district court.").

[47] *See, e.g.,* ALA. R. CIV. P. 27(a)(1) (allowing pre-suit discovery for "a person who desires . . . to obtain discovery under Rule 34 or Rule 35 regarding any matter that may be cognizable in any court of this state."); N.Y.C.P.L.R. § 3102(c) ("Before an action is commenced, disclosure to aid in bringing an action . . . may be obtained, but only by court order."); OHIO CIV. R. P. 34(D)(1) ("[A] person who claims to have a potential cause of action may file a petition to obtain discovery as provided in this rule."); PA. R. CIV. P. 4003.8 ("A plaintiff may obtain pre-complaint discovery where the information sought is material and necessary to the filing of the complaint and the discovery will not cause unreasonable annoyance, embarrassment, oppression, burden or expense to any person or party."); TEX. R. CIV. P. 202.1 (allowing pre-suit depositions "to investigate a potential claim or suit"); *see generally* Scott Dodson, *Federal Pleading and State Presuit Discovery*, 14 LEWIS & CLARK L. REV. 43 (2010).

[48] Such pre-suit discovery in state courts can also conceivably be used to obtain facts in support of RPA claims to extent that the facts underlying the state and federal claims overlap. Note that some federal courts have held that pre-suit discovery petitions in state court are not removable to federal court because such petitions do not constitute a "civil action" under the removal statute. *See, e.g., Young v. Hyundai Motor Mfg. Ala., LLC,* 575 F. Supp. 2d 1251, 1254 (M.D. Ala. 2008); *McCrary v. Kansas City S. R.R.*, 121 F. Supp. 2d 566, 569 (E.D. Tex. 2000).

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Minimum Advertised Pricing Programs: Practical Pointers in the Wake of *Leegin*

By: Patricia A. Sullivan and Elizabeth H. Kelly

Minimum advertised pricing policies ("MAP") have become one of the most important tools in the kit for manufacturers or distributors[1] of products seeking:

- to preserve an investment in brand, quality, luxury, innovation or sophistication;
- to incentivize retailers to invest in product display, education, sales and service training for employees; and
- to prevent free riding.

The increase in the use of MAP policies in the aftermath of the Supreme Court's decision in *Leegin Creative Leather Products Inc. v. PSKS Inc.*,[2] is directly related to the post-*Leegin* confusion[3] caused when many of the states declined to follow it. As a result, MAP policies are a safer way to achieve the goals generally used to justify resale price maintenance ("RPM"). MAP policies are now common in industries ranging from electronics to sporting goods, computers to plumbing equipment.[4]

MAP policies arise in a vortex of vertical and horizontal relationships that are rife with antitrust risk – therefore, it is critical for antitrust advisors to be fully aware of the complex and contradictory law in this area so that the policy adopted minimizes risk while maximizing the goals that justify it. Manufacturers of products resold to consumers by retailers they cannot fully control not only want an effective distribution system, but also one that carries a predictable level of antitrust risk. This need for certainty can be satisfied by the careful implementation of an antitrust compliant MAP policy.

What is MAP? A minimum advertised pricing policy is an attempt by the manufacturer of a product to control the advertising of its product by the reseller, focused on the price. Generally a MAP policy specifies a price below which certain products cannot be offered in advertisements. Sometimes control over advertising content is linked to cooperative advertising payments – the manufacturer interferes with the reseller's advertised price only when the manufacturer is paying for the advertising. However, more commonly the MAP policy broadly prohibits display of a price below a specified level in conjunction with the name of the product. A MAP policy may also police advertising content that denigrates or commoditizes the product.

Importantly, a MAP policy does not stipulate what the reseller's sales price should be. Moreover, a MAP policy can, and should, be implemented as a unilateral *Colgate*[5] policy, avoiding the formation of any agreement between the manufacturer and retailer. An effective MAP policy impacts the amount of intrabrand price competition associated with the product.

MAP policies achieve important procompetitive business goals. First, MAP policies protect the brand investment by the manufacturer. A MAP policy allows the manufacturer to avoid the stigma of being the loss leader and to protect product investment from being undermined by discount advertising to drive up traffic.[6] MAP policies are especially important for high-end, luxury or big ticket products because of greater need for retailer investment in sales and service.[7] When the manufacturer cannot protect its investment in quality or innovation, such investment is stifled, consumers are harmed and interbrand competition is impaired.[8]

Second, MAP policies protect retailers from "free riders." Luxury and high end products rely on retailers to display and present the product to the consumer. If the consumer can shop and choose the product through the efforts of the retailer who has invested in the presentation of the product, and then troll the internet for advertisements displaying the product for less, the retailer who invested in the product will loose the sale to the free rider.

Labyrinthine State of the Law of Vertical Pricing Post-*Leegin*. Because MAP policies affect vertical pricing, a tour of the post-*Leegin* landscape is advisable.

One commentator has wryly stated that "the path to establishing an RPM program is not a clear, unobstructed, or safe one.[9] *Leegin*

overturned the 96 year *per se* ban on minimum RPM,[10] laying out procompetitive justifications for RPM, including encouragement of retailer investment and market entry, discouragement of free riding.[11] The opinion also lists anticompetitive effects, including manufacturer and retailer cartels, and the risk that dominant retailers or manufacturers will implement RPM that impairs interbrand competition.[12] Red flags for these anticompetitive effects include widespread use of RPM in the industry, retailer-initiated RPM, and retailer or manufacturer market power.[13] After noting these potential justifications and anticompetitive effects, the Court stepped away, leaving to the lower courts the job of fashioning a workable a rule of reason analysis.

Since *Leegin*, federal courts interpreting federal law have focused on market power and whether the RPM is retailer-driven.[14] One federal RPM challenge that survived the pleading stage, the Babies "R" Us cases, involved coercion by the dominant retailer.[15] Where the plaintiffs alleged that the manufacturers imposed RPM against self-interest and the dominant retailer used its power to induce them to do it by threats of termination, the plaintiffs sufficiently alleged an antitrust violation.[16]

This relative clarity in federal RPM law contrasts with what has happened in the states. Thirty-seven attorneys general argued in *Leegin* to preserve the *per se* prohibition on RPM.[17] Since *Leegin*, state enforcement poses serious, indeed, unacceptable antitrust risks for manufacturers considering minimum RPM. For example, in New York, the Attorney General sued Tempur-Pedic over a *Colgate* policy of suspending retailers who did not adhere to suggested resale prices; the court dismissed because the complaint failed to demonstrate an agreement.[18] And in California, the Attorney General sued beauty product makers, claiming that they had agreements with retailers that prohibited the prices below the suggested retail price.[19] While these states acknowledge the unilateral *Colgate* right to announce a policy and then refuse to deal with violators, New York's decision to initiate the Tempur-Pedic case makes clear that the states believe that a unilateral *Colgate* RPM policy can easily drift into an illegal RPM agreement.[20]

Despite these risks, since *Leegin,* industry observers have concluded that many manufacturers have instituted pricing minimums for either advertising or sales.[21] However, an RPM program that is part of a national or internet-based distribution scheme runs significant risks due to the enforcement philosophies of the states.

Legal Analysis of MAP Policies. It is well settled that cooperative advertising conditioned on use of a discount price in the advertising copy is subject to the rule of reason.[22] In 1992, the Commission acknowledged that unilaterally terminating a dealer for advertising below suggested prices is less competitively threatening to interbrand competition than unilaterally terminating a dealer for failing to follow a suggested resale price.[23] As long as the policy is supported by procompetitive justifications, and the market is competitive, a *Colgate*-based MAP policy should be permissible.[24]

In 2000, the FTC challenged a MAP policy of the five largest distributors of compact discs, resulting in consent orders halting the MAP policies,[25] because the companies had used collective market power to squelch discount retailers by conditioning cooperative advertising payments on the advertising of low prices. It was also troublesome that retailers had requested the MAP policy.

The most significant antitrust risk for a post-*Leegin* MAP policy is the danger that it will arise from or cause communications among horizontal competitors, at either the manufacturer or retailer level. Then, the benign rule of reason is replaced by the *per se* prohibition on horizontal price agreements. For example, the National Association of Music Merchants facilitated the adoption of MAP policies among manufacturers and retailers.[26] These horizontally driven policies resulted in a strongly worded press release when the FTC announced the Consent Decree: "The strong terms of the Commission order announced today will protect consumers from paying higher prices by ensuring that NAMM does not facilitate anticompetitive agreements or coordination."[27]

The states have focused on MAP policies. In 2008, New York, Illinois, and Michigan sued the furniture maker Herman Miller.[28] The complaint alleged that Herman Miller's MAP policies were anticompetitive because they established minimum prices below which retailers were prohibited from advertising Herman Miller chairs. The complaint was ambiguous as to whether it alleged a *per se* violation. Nevertheless, shortly after the filing, Herman Miller agreed to pay $750,000 and to refrain from entering into agreements with dealers to fix advertising prices.[29]

Worldhomecenter.com, Inc. v. L.D. Kichler Co., Inc.,[30] involved a MAP policy that amounted to a unilateral refusal to sell to retailers that advertised prices below the policy price. While the New York court found no allegation of an agreement, it declined to dismiss the claim that a unilaterally announced MAP policy could constitute vertical price fixing. While this holding has been characterized as dicta[31] and the opinion lacks any analysis to explain the conclusion, the case illustrates how the unsettled state of the law poses risks, even for what appears to have been a *Colgate*-based policy.

Conclusions and MAP Practice Tips.

These cases suggest four antitrust danger zones for a MAP program:

1. Horizontal – the implementation of the MAP will lead to "chatter" among dealers and retailers or collusion among upstream manufacturers. If the retailers coordinate to inform the manufacturer of competitors who are deviating from the policy, the policy is vulnerable to challenge.

2. Vertical – unless crisply and unilaterally imposed by the upstream firm, the MAP policy may drift into a vertical agreement between the manufacturer and retailer.

3. A MAP policy may be so focused on the selling price, as opposed to the advertising price, that it is recast as RPM.[32] Drawing the difference between advertised price and sales price can be particularly difficult for internet-based retailers.[33]

4. MAP policies are more risky in highly concentrated markets or markets with either a dominant manufacturer or a dominant retailer.

In light of this uncertain law, practice tips for a manufacturer seeking to adopt of MAP policy include:

- Be sure the MAP policy is implemented by the entity that launches the product in the stream of distribution and that it is being implemented for the purpose protecting the investment of that originating seller in developing brand recognition, luxury status and reputation or raising expectations of quality in consumers.
- Adopt a MAP policy that is crisp and clear, through a written communication supplemented by FAQs to explain how the policy will work. Before rolling the policy out, be sure to think through such scenarios as:
  - Can internet retailers use "click for price" as a way to advertise a price below the minimum? Many MAP policies prohibit this practice.
  - How does a store-wide sale affect the products subject to the MAP policy? Many MAP policies prohibit the use of the product name or logo to advertise the store wide sale.[34]
- Clearly lay out the sanctions that will be implemented when violations of the policy are detected and implement them as soon as the violation is confirmed.
- Be clear that the policy cannot be the subject of discussion or negotiation over the price. If a violation is detected, discuss only whether the advertisement found was in fact run by the retailer to be sanctioned.
- Clearly specify that the retailer remains free to set its own price.
- Refuse to communicate with retailers complaining about the advertising of other retailers -- be clear that retailers should not discuss the pricing of their competitors among themselves and refuse to permit them to discuss it with the manufacturer.
- Adopt a strategy for monitoring compliance prior to rolling out the MAP policy. This may include an internet company that scours the internet for below-MAP advertising prices. Also adopt a plan for periodic checks of other forms of advertising.[35]
- Be aware that proper implementation of a MAP policy has transactional costs[36] and be sure that the pro-competitive justifications truly promise sufficient benefits to offset those costs.

Minimum advertised price policies are a safer than RPM because they are not agreements to restrain vertical prices and are tested under the rule of reason. Nevertheless, they are exposed to antitrust challenge when they have anticompetitive effects and are not properly designed and implemented.

[1] The originating seller of a product, which might wish to affect the downstream pricing of its product, could be a manufacturer, a distributor or some other kind of entity. For convenience, in this article, we will refer to the originating seller as the "manufacturer." We will refer to the entity subject to the MAP policy or other vertical price restraint as the "retailer."

[2] 551 U.S. 877 (2007).

[3] *Leegin* has been the subject of considerable commentary and criticism. *See, e.g.*, W. Grimes, "A Dynamic Analysis of Resale Price Maintenance: Inefficient Brand Promotion, Higher Margins, Distorted Choices, and Retarded Retailer Innovation," 55 The Antitrust Bulletin 101 (Spring 2010).

[4] A. Israeli, E. Anderson, A. Coughlan, "Determinants of MAP Violations," at 3 (September 2011), *available at* http://www.kellogg.northwestern.edu/faculty/anderson_e/htm/PersonalPage_Files/Papers/Determinants_of_MAP_Violations.pdf

[5] In *United States v. Colgate & Co.*, 250 U.S. 300 (1919), the Supreme Court held that a manufacturer can unilaterally announce its resale prices in advance and refuse to deal with those who fail to comply.

[6] *In the Matter of U.S. Pioneer Electronics Corp.*, 115 F.T.C. 446, 450-51 (1992) (lays out business justification for unilateral MAP policy accepted by FTC as legitimate).

[7] *Id.* at 451.

[8] *Id.* at 450-51.

[9] S. Romano, "Resale Price Maintenance For Beginners: Beware of the Pitfalls," 55 The Antitrust Bulletin 513, 537 (Summer 2010).

[10] *Leegin*, 551 U.S. at 899.

[11] *Id.* at 889-892.

[12] *Id.* at 892-894.

[13] *Id.* at 897-898.

[14] *PSKS, Inc. v. Leegin Creative Leather Products, Inc.*, 615 F.3d 412, 418 (5th Cir. 2010) (amended complaint dismissed because PSKS failed to allege a plausible relevant market that included reasonably interchangeable products over which the defendant had power); *Jacobs v. Tempur-Pedic Int'l, Inc.*, 626 F.3d 1328, 1339-1340 (11th Cir. 2010) (affirming dismissal of complaint filed by customers against Tempur-Pedic for enforcing RPM agreements with its distributors due to failure to plausibly allege a relevant product market in which Tempur-Pedic had market power or injurious exercise of market power such as restricted output or supracompetitive prices); *see also In the Matter of Nine West Group, Inc.*, FTC Docket No. C-3937, slip. op. at 17 (May 6, 2008) (petition to FTC to set aside RPM prohibitions in pre-*Leegin* consent decree granted in part, because Nine West lacked market power and because its retailers were not the source of the RPM).

[15] *McDonough v. Toys "R" Us*, 638 F.Supp.2d 461 (E.D. Pa. 2009); *Babyage.Com, Inc. v. Toys "R" Us*, 558 F. Supp.2d 575 (E.D. Pa. 2008), *reconsideration denied*, 2008 WL 2644207 (E.D. Pa. 2008).

[16] *Id.* at 582-583.

[17] *See* Brief for the States of New York, Alaska, Arkansas, Connecticut, Delaware, Florida, Hawaii, Idaho, Illinois, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nevada, New Hampshire, New Jersey, New Mexico, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, South Dakota, Utah, Vermont, Washington, West Virginia, and Wyoming as Amici Curiae Supporting Respondent, *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 127 S. Ct. 2705 (2007) (No. 06-480), 2007 WL 621851.

[18] *People v. Tempur-Pedic Int'l. Inc.*, No. 400837/10, slip. op. at 14 (N.Y. Sup. Ct., N.Y. Cty., Jan. 14, 2011).

[19] *People v. Bioelements, Inc.*, Docket No. 10011659 (Cal. Super. Ct. Riverside County, Dec. 30 2010) (Complaint); *People v. Dermaquest, Inc.*, Docket No. RG10497526 (Cal. Super. Ct. Alameda County, Fed. 2010) (Complaint). In both cases, the manufacturers settled.

[20] For example, in *Isaksen v. Vermont Castings, Inc.*, 825 F.2d 1158, 1164 (7th Cir. 1987), the manufacturer announced a minimum resale price, but told retailers they could charge whatever price they chose. However, when competitors of a price cutter began to complain, the manufacturer engaged in dialogue with the violating retailer, threatening and harassing. Ultimately the retailer raised the price. The court found that the policy was protected by *Colgate*, but the coercive tactics implicitly formed an agreement by "conduct in lieu of promissory language."

[21] Gundlach, "Overview and Contents of the Special Issue: Antitrust Analysis of Resale Price Maintenance After *Leegin*," 55 The Antitrust Bulletin 1, 11-13 (Spring 2010).

[22] *Nissan Antitrust Litigation*, 577 F.2d 910, 917 (5th Cir. 1978). *See also Advertising Checking Bureau, Inc.*, 109 F.T.C. 146 (1987).

[23] *In the Matter of U.S. Pioneer Electronics Corp.*, 115 F.T.C. 446, 466 (1992).

[24] *Id.* at 458, 466. *See also* Remarks of J.T. Rosch, Commissioner, FTC, "Current Issues in Competition and Consumer Protection Enforcement in the Retail Sector," at 21 (November 10, 2010) (hereinafter cited as "Rosch"), *available at* http://www.ftc.gov/speeches/rosch/101110roschretailerspeech.pdf.

[25] *See, e.g., In re BMG Music*, Docket No. FTC File No. 971-0070, C-3973 (F.T.C. 2000); *see also In re Compact Disc Minimum Advertised Price Antitrust Litig.*, 138 F. Supp. 2d. 25 (D. Me. 2001);.

[26] *In re National Assoc. of Music Merchants*, FTC File No. 001-0203 (Complaint) (March 4, 2007).

[27] Press Release, FTC, "National Association of Music Merchants Settles FTC Charges of Illegally Restraining Competition" (Mar. 4, 2009), *available at* http://www.ftc.giv/opa/2009/03/namm.shtm.

[28] *New York v. Herman Miller, Inc.*, No. 08-CV-02977, (S.D.N.Y. 2008).

[29] *Id.* (Consent Decree filed March 25, 2008).

[30] No. 09-CV-020 (DRH)(ETB), 2009 WL 936675 (E.D.N.Y. March 31, 2009).

[31] *See* 4B N.Y. Prac., Com. Litig. in New York State Courts § 89:22 (3d ed.).

[32] Some commentators believe that the state anti-RPM enforcement commitment will continue to conflate MAP policies with RPM. J. Mitnick, J. Lavelle, W. Reiss, O. Smith, "A Commentary on Current State Enforcement Policy for RPM on Life Support From Leeginair's Disease: Can the States Resuscitate Dr. Miles?", 22 Antitrust 63 & N.2 (Summer 2008). *See also* Rosch at 22. The viability of this treatment is questionable because a true MAP policy leaves the retailer free to sell below the suggested advertised price. *See, e.g., Blind Doctor, Inc. v. Hunter Douglas, Inc.,* 2004 U.S. Dist. LEXIS 18480, at *6 (N.D. Cal. Sept. 7, 2004) (MAP policies prohibiting the printing of discounts that exceeded the maximum discount did not constitute per se violation of the Sherman Act because they did not dictate the actual prices retailers could charge).

[33] This risk is exacerbated for internet sellers for whom the advertisement of the price and the charging of the price are virtually the same conduct. Internet resellers have tried to use such devices as "click for price" to circumvent the MAP policy. However, it is increasingly common for the "FAQs" underlying the MAP policy to make clear that "click for price" cannot be used as a way to circumvent the prohibition on advertising. Thus, the consumer chooses the product and "puts it in the basket," presumably accepting the obligation to pay the MAP policy price. Further discounts, such as those based on retailer loyalty programs, may be applied at checkout, without violating the MAP policy. *See generally* Rosch at 22.

[34] However, if the consumer chooses the product, the retailer may apply the sales discount at the register. This dichotomy clearly illustrates that the MAP policy affects the advertising of the discount, but not the sale at the discounted price.

[35] For a discussion of the industry that has sprung up to monitor the internet for violators of MAP policies, *see* J. Pereira, "Discounters, Monitors Face Battle on Minimum Pricing", Wall Street Journal (Dec. 4, 2008), *available at* http://online.wsj.com/article/SB122835660256478297.html.

[36] Manufacturers contemplating the unilateral adoption of a MAP policy need to be cognizant of the need to invest time and money in establishing a clear policy, creating a method for dealing with questions, and monitoring the internet and other advertising for violations, and when violations are found evenhandedly and without negotiation or agreement imposing previously established sanctions.

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Pricing Conduct Committee Pricing Fundamentals Series Program I: Pricing Related to Other Offerings

By: Chahira Solh

On February 1, 2012, the ABA Section of Antitrust's Pricing Conduct Committee presented the first program in its Pricing Fundamentals Series. Program I provided an overview of pricing tied to other offerings, focusing on tying, full-line forcing, loyalty and market share discounts, and bundling. Kathleen Foote, of the California Attorney General's Office, and Scott Martin, of Greenberg Traurig, LLP, discussed the basics of this area of the law. The discussion was moderated by Mary Marks, Vice-chair of the Pricing Conduct Committee

Mr. Martin started by outlining the law in this area, including tying, full-line forcing, loyalty and market share discounts, and bundling. Various of these types of prices tied to other offerings can be challenged under Section of the Sherman Act, Section 1 of the Sherman Act, Section 3 of the Clayton Act, Section 5 of the FTC Act, state antitrust laws, and state unfair competition laws. Generally, courts have looked at market power when analyzing whether this pricing conduct is anticompetitive.

Tying

Mr. Martin explained the factors to be taken into consideration when examining tying arrangements. Tying is a vertical restraint where the supplier has made it so the ability to purchase one product (tying product) is conditioned on the purchase of another distinct product (tied product) (*e.g.*, shampoo and conditioner). Where the purchaser needs the tying product and the seller has market power, the purchase of the tied product can be forced.

The seminal case on tying issues is *Jefferson Parish Hosp. Dist. No. 2 v. Hyde,* 466 U.S. 2 (1984), where there was alleged tying of anesthesiology services to other hospital services. In that case, the Court held that tying is *per se* unlawful if (1) "separate demand" exists for products; (2) there is substantial foreclosure in the tied product market; and (3) the seller has market power in the tying product market. Separate demand for a product exists if the tying product is separate and distinct from the tied product. Substantial foreclosure is generally met by showing that a substantial amount of sales would have occurred but for the tying. A 30% market share is a good indicator that the company has market power. Many lower courts have examined a variety of business justifications with respect to tying arrangements. Thus, a quasi-*per se* rule has developed, employing factors used in a Rule of Reason analysis.

Ms. Foote noted that the National Association of Attorneys General has adopted the Vertical Restraints Guidelines, which are advisory in nature. The Vertical Restraints Guidelines reiterated the holding in *Jefferson Parish* but also include discussion of the pragmatic, rule of reason inquiry.

Tying arrangements exist in a variety of sectors, and are sometimes anticompetitive. Some market segments where tying arrangements can be found include technological markets and aftermarkets. Further, an analysis of issues related to full-line forcing turns on these elements of tying law. In full-line forcing, a company forces its distributor to carry an entire line of products instead of just certain products from that line. However, if there is no harm to interbrand competition, this type of arrangement may not pose concerns.

Tying issues can often arise when government entities bid out public works projects. In many situations, the government entity asks for bids for project and specifies a particular product to be used in the project. The company that makes that particular product automatically gets market power because of this designation. Sometimes these companies then require purchase of the other components needed for the project as the only way that a bidder is able to buy the government specified product. Ms. Foote discussed cases involving these issues that her office has litigated, including one where a municipality was bidding out a project for traffic light switches. The municipality specified a certain control box to be used in the project, which was only manufactured by one company and

distributed through another. The control box manufacturer and distributor sold the control box at a fair price but required the purchase of other light switch components at extremely high prices. This case went to trial, and Ms. Foote's office was able to prove that the tying arrangement was anticompetitive.

Loyalty and Market Share Discounts

Mr. Martin next outlined loyalty and market share discounts. He noted that loyalty discounts or rebates are offered to distributors/retailers in return for guaranteeing a minimum purchasing volume or percentage. Market share discounts are offered to distributors/retailers in return for guaranteeing purchases or shelf space on par with the producer's market share.

These types of discounts are not tying, not exclusive dealing, and not bundling. However, they are often part of bundling as a commitment to buy at certain levels may be necessary to get the best prices. Some important cases to keep in mind, in addition to the general principles in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), *are Concord Boat Corp. v. Brunswick Corp.*, 207 F.3d 1039 (8th Cir. 2000) and *In the Matter of Intel Corp.* (FTC consent order in 2010). Courts will look at the market conditions and whether any competitors are offering similar types of loyalty discounts. Further, courts will look to see whether the distributors/retailers would purchase the share amount regardless of any discounts.

Bundling

Mr. Martin then explained that bundling is when a seller provides discounts to a buyer on a product if the buyer purchases two or more different products together. There is no element of forcing (as with tying) in a bundling arrangement. As with all types of discounts, it is important to determine whether the supplier has market power.

There are several cases to keep in mind when counseling on this issue. In *LePage's Inc. v. 3M*, the Third Circuit held that it was unlawful for supplier with market power to bundle products if a competing supplier of less than all products could not profitably make a comparable offer. (324 F.3d 141 (3rd Cir. 2003). In *LePage's*, 3M, which had monopoly power, was bundling products (at above cost) but the arrangement was found to be anticompetitive. The Third Circuit reasoned that when bundles are offered by a monopolist, these types of bundles may foreclose the market to a competitor (who need not necessarily be an equally efficient one) who does not make as many products.

In *Cascade Health Solutions v. PeaceHealth*, the Ninth Circuit held that bundling is unlawful if, attributing all discounts only to competitive products, the imputed price for the competitive product would be below average variable cost to produce and cannot profitability be met by a hypothetical equally efficient competitor. (515 F.3d 883 (9th Cir. 2008)).

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Pricing Conduct Committee: Pricing Fundamentals Series Program 2: Resale Pricing Restraints

By: Christie L. Stahlke

On February 2, 2012, the ABA Section of Antitrust's Pricing Conduct Committee presented the second program in its Pricing Fundamentals Series. Program 2 discussed the use of retail pricing restraints and restraints on price advertising. Warren Grimes, Professor of Law at Southwestern Law School, and Tasneen Chipty, Managing Principal at Analysis Group, discussed the applicable law and considerations for prosecuting and defending these claims. Bob Hubbard, Chair of the Pricing Conduct Committee, moderated.

Resale Price Maintenance

Mr. Hubbard opened the discussion by asking Mr. Grimes to describe why parties use resale price maintenance ("RPM"). Although RPM is often welcomed by manufacturers, Mr. Grimes first explained that not all manufacturers or retailers favor RPM. For example, manufacturers that can compete on price would have less incentive to impose RPM. Also, manufacturers with a strong brand image (e.g., Crest, Tide) may not favor RPM because every retailer already has an incentive to carry their popular product. According to Mr. Grimes, the more likely candidate for RPM is a manufacturer with a weaker brand who does not wish or is unable to compete on price.

Ms. Chipty added that manufacturers who offer products that would benefit from a customized or tailored retail service situation are also likely to consider RPM. In *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007), Leegin's story was that its products were best sold through smaller retailers that provided customer service in a friendly environment. Ms. Chipty proposed that Leegin was a fairly strong brand using an incentive scheme to induce retailers to provide their ideal sale strategy. The operative question was whether RPM was the best way to achieve this result, or if there was another way. In Mr. Grimes's view, Leegin used RPM to protect higher manufacturer profit margins, not as a way to incentivize a certain sales experience. He did not necessarily agree that Brighton was a strong brand the way Coach is, for example. Since some have suggested that RPM is usually associated with weaker, more insecure brands, he was not convinced by Leegin's story.

Ms. Chipty opined that not every instance of RPM represents an exercise of ill will towards consumers and an attempt to unlawfully raise prices. In order to establish that a company like Leegin used RPM for anticompetitive purposes, it is necessary to ask the "usual" questions that go along with an antitrust inquiry, such as assessment of market power. Mr. Grimes countered that manufacturers do not operate in terms of good and evil; they make decisions to optimize profits. If manufacturers have a choice between using promotional allowances and RPM—either of which would promote the offering of additional services to some degree—they may select RPM because unlike promotional allowances, it may encourage better dealer services while increasing margins for both the manufacturer and the retailer. Ms. Chipty granted that there are some circumstances where RPM would be easier than a promotional retail program, which would require a close monitoring process.

Mr. Grimes clarified that selling more of a product is not the only way of increasing profits. In some cases, selling less of a product at a higher price will lead to increased profits. He noted that RPM is usually associated with higher priced products. For those manufacturers looking to place a premium product, RPM is attractive for marketing purposes because it creates an incentive for the retailer to market the product notwithstanding the higher retail price.

Ms. Chipty added that a manufacturer with market power does not need RPM to charge retailers higher prices. What the manufacturer really wants is intense competition among retailers to widely distribute its product.

Mr. Grimes proposed that a market power screening test would not be helpful in the context of brand-selling. RPM and other vertical restraints can be a way of exploiting brand power. RPM also creates incentives for onsite retail market power. An example of this would be a pharmacist

that places a display of a toothpaste brand in a prominent position. In that example, RPM would create a degree of instant onsite market power for that brand. As a result, Mr. Grimes doubted whether a market power screening test would be all that useful. A market power test is also problematic when use of RPM becomes widespread in an industry category. The market share of a particular defendant that imposes RPM does not account for the overall anticompetitive effects when other rival brands are also imposing RPM. Ms. Chipty said that there was well-established thinking on market definition to assess the competitive effects of conduct and that by those methods, Crest and other leading brands could be in the same antitrust market. She asked Mr. Grimes why those methods should not apply to assessing the anticompetitive effects of RPM. Mr. Grimes acknowledged that Ms. Chipty view was the orthodox view in the literature and the courts.

RPM vs. Alternatives

Mr. Hubbard then asked the panelists to compare RPM with exclusive dealing arrangements or other vertical pricing restraints. Mr. Grimes explained that RPM is a way of controlling the retail price in an open distribution system, whereas exclusive dealing more effectively addresses the issue of free riding. The disadvantage of exclusive dealing is that it presupposes a limited retail network. RPM, on the other hand, is attractive to manufacturers who want the control over price, but still want a broad distribution network.

Ms. Chipty addressed the issue of RPM leading to higher prices. She recognized that few would dispute that RPM leads to higher prices. Thus, she emphasized that a rule of reason treatment of RPM requires a thorough analysis of whether there are benefits that flow from RPM, and whether those benefits offset the harm. She agreed that the analysis must also consider whether there is a better way to deliver the same benefits, such as exclusive dealing. Ms. Chipty concluded that the outcome would be dependent on the empirical evidence.

Mr. Grimes discussed the free riding issue where consumers might visit a brick and mortar store to inspect a brand, but then make the purchase online. But Mr. Grimes also noted the opposite effect, where consumers shop for items on the Internet, then go out to brick and mortar stores to purchase and receive the item quickly. This enters into the RPM debate because free riding on presale services is one customary justification for RPM. Mr. Grimes suggested that promotional allowances targeted to those that provide presale services were the better way to prevent free riding.

Mr. Grimes suggested as a practice tip that attorneys carefully examine their clients' rationale for imposing RPM and walk through with them other options that are less risky from an antitrust perspective, such as promotional allowances.

Ms. Chipty countered that promotional allowances still come with incentive problems. Brick and mortar stores with promotional allowances will put in less effort over time if consumers continue to take advantage of the presale services in person, but make purchases online. For promotional allowances to be effective, they must be tied to sales generation, or the incentive will erode over time. She also pointed out that promotional allowances themselves raise the manufacturers' costs and could also push prices up. Mr. Grimes pointed out that promotion allowances can operate efficiently when they are based on a percentage of sales and would avoid the anticompetitive effects of RMP.

Current Federal and State Law on RPM

Mr. Hubbard asked Mr. Grimes to provide an overview of current federal and state law concerning RPM. Mr. Grimes began with the U.S. Supreme Court's decision in *Leegin* as the latest pronouncement on RPM under federal law. The *Leegin* decision overturned the per se rule against vertical minimum price fixing and replaced it with a rule of reason analysis. Mr. Grimes explained that the new rule has generated a great deal of debate as to where federal law should go next. Some propose a structured rule of reason, such as Christine Varney, former Assistant Attorney General for the Antitrust Division, who gave a speech about the possibility of a structured rule of reason.

Mr. Grimes pointed out that state law is not always in sync with federal law, which causes difficulty when advising clients. For example, California continues to employ the per se rule under state law. Clients may wish to consider structuring their RPM to take advantage of the *Colgate* doctrine, which provides a window for manufacturers to impose RPM unilaterally. This is

likely to be a valid defense under federal law and in most states.

Building Evidence in RPM Cases

Although Ms. Chipty declined to opine on the state of federal and state law on this issue, she offered insight into the types of evidence that might play a role in evaluating RPM. She thought that the *Leegin* decision provided a great deal of guidance with regard to evidence. She quoted Justice Kennedy who said in Leegin that the Court in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911), "failed to discuss in detail the business reasons that would motivate a manufacturer situated in 1911 to make use of vertical price restraints." In terms of building evidence, the first step is to look for information relevant to the business in question by reviewing business documents. Specifically, the questions to ask are what services were gained, what branding was achieved, were there inventory issues, what benefits did the manufacturer gain by giving retailers a bigger margin, and, importantly, were there other, cheaper ways to deliver the same results? Second, to the extent it is possible to build evidence from the markets, that information should be compiled. There may be a situation where a manufacturer used RPM in some places, but not others; at one point in time, but it eventually stopped the practice. The idea is to look for natural experiments in the manufacturer's data to determine whether one can assemble systematic evidence of the effects of RPM. Third, there is the usual inquiry of market power and market structure. This might include a market definition analysis. With a rule of reason analysis, the bottom line is that it must assess the impact on customers.

Mr. Grimes prefaced his response by saying that he holds strong views on this issue. He posited that since the *Sylvania* decision in 1977, the Supreme Court has "issued a pass" to use the free rider argument in connection with vertical restraint cases, including RPM. As a result, attorneys look for free riding explanations even when that is not the primary reason for imposing RPM. The risk for the defense is that the plaintiff's attorney will then target that argument and demonstrate why it is not the real motivation behind RPM. The candor and authenticity of any explanation for RPM thus becomes critical. Ms. Chipty agreed that the fight during litigation would be over whether the presale services or other extra efforts by retailers were in fact essential, or whether they were concocted.

Mr. Grimes pointed to *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717 (1988), where the discounter was just as active in providing onsite presale demonstrations—perhaps even more so—than the defendant. The discounter would go to the customer's business premises to demonstrate the product. Thus, although the defendants prevailed in that case, the free riding explanation was not convincing. The actual evidence showed that the discounter was anything but a free rider. This case underscores the importance of putting forth genuine reasons for using RPM.

Ms. Chipty referenced the extensive "back and forth" that has occurred in court cases and academic journals, but also noted the lack of systematic evidence to support the strong opinions. She thought that the next few years might bring natural experiments to examine in order to generate empirically-based opinions on the pros and cons of RPM.

Mr. Grimes cited empirical evidence available from the days of fair trading laws, where prices paid by consumers in states that allowed RPM were higher than those paid by consumers in states that did not allow it. Still, that evidence does not address whether the manufacturers imposing RPM were providing enhanced services that consumers valued.

RPM and Innovation

Mr. Grimes argued that RPM can suppress or delay innovative retailing. Internet retailing is threatening traditional retailing methods, which is causing increased support for RPM among traditional retailers. Mr. Grimes asserted that one of the most pervasive harms of RPM is that it slows evolution of innovative discounting and other efficient retail strategies.

RPM and Globalization

Mr. Hubbard asked the panelists what effect, if any, globalization is having on the RPM debate. Ms. Chipty suggested that the international experience might be an interesting way to look for evidence from a litigation perspective. As markets become global, RPM might be easier to implement than promotional allowances. This could change over time, however, if there are more markets to consider since the manufacturer would have to set different price structures for different markets. In addition, the internet and other creative ways for firms to

sell would allow consumers to arbitrage across different geographic markets, which could quickly undo an RPM scheme.

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