The Soul of Franchising
THE FALLOUT EIGHT YEARS AFTER LEEGIN: WHEN AND WHERE CAN FRANCHISORS FIX THE PRICES CHARGED BY FRANCHISEES?

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BACKGROUND: SECTION 1

Joint Action

Contract, Combination or Conspiracy
BACKGROUND:

Horizontal and Vertical Restraints
Horizontal/Vertical and Interbrand/Intrabrand Schematic
BACKGROUND:

The *Per Se* Rule

The *Per Se* Rule
BACKGROUND:

The Rule of Reason
1977
First Nail in the Coffin of the *Per Se* Rule on Vertical Restraints.

- *Continental TV, Inc. v. GTE Sylvania, Inc.*
- Territorial and customer restraints evaluated under Rule of Reason
- Interbrand versus intrabrand relevant market effects
The *Per Se* Rule on Vertical Restraints Continues to Expire

- Tying arrangements become effectively Rule of Reason
The Rule of Reason Revolution Consumes Maximum Vertical Price Fixing

Maximum Resale Price Maintenance ("RPM")

*State Oil Co. v Khan* (1997)
The Tsunami: the Final Shoe Drops

BACKGROUND: Minimum RPM

- Up to 96 years of *per se* prohibition of minimum RPM
- *Dr. Miles Medical Co. v. John D. Park & Sons Co.* (1911)
- *United States v. Parke, Davis & Co.* (1960)
Leegin: The Facts

- Defendant announced new policy to terminate retailers who discounted its “Brighton” line.
- Plaintiff continued to discount
- Manufacturer terminated supply to plaintiff
*Leegin*: Holdings Below

- District court refused Rule of Reason justifications and expert testimony because of *per se* rule
- Fifth Circuit court affirmed
**Leegin: The Supreme Court**

Court votes 5-4 to overrule *per se* rule for minimum RPM
Leegin: The Decision’s Three Pillars

A. *Dr. Miles* was not based on economic effects
B. Minimum RPM has some pro-competitive justifications and effects
C. *Stare decisis* did not justify continuing an outdated rule.
Leegin: The Four Key Pro-Competitive Justifications

A. Encouraging retailers to invest in service and promotion
B. RPM provides more brand diversification
C. Avoidance of free riding by discounting retailers
D. RPM may encourage market entry
Leegin: Three Plus Factors Weigh in Favor of Plaintiffs under the Rule of Reason

A. Where many manufacturers in an industry adopt minimum RPM
B. Where minimum RPM results from horizontal retailer cartel pressure
C. Where the manufacturer has substantial interbrand market power
Leegin:
The Court left it to lower courts to flesh out the balance
**Leegin in the Federal Courts to Date**

As expected, fewer minimum RPM cases

- *Toledo Mack Sales and Service Inc. v. Mack Trucks, Inc.* (3d Cir. 2008) – possible dealer cartel
- *Babyage.com, Inc. v. Toys “R” Us, Inc.* (ED Pa 2008) - Defendant’s powerful market position
Defense Victories are the Norm

Examples:

A. *Leegin* itself

B. *Columbus Drywall & Insulation, Inc. v. Masco Corp* (N.D. Ga. 2009)

C. *Jacobs v. Tempur-Pedic Int'l., Inc.* (11th Cir. 2011)
Minimum RPM: What Direction to Take?

• *Leegin* provides little guidance
  – Increased litigation and liability risks because fewer early dismissals?
• ROR does not ensure defendant win
  – Unclear pro-competitive justifications
• State antitrust laws occasionally produce a different result
The States: The Crucial Arena

- State RPM law is not preempted by federal law
- Under most state laws, federal precedent is persuasive but has no direct effect
- 19 states by statute or court ruling do or may prohibit minimum RPM
State RPM Laws

• State examples
  – California: statutory language; *Mailand v. Burckle* (Cal. 1978) still controls
  – Maryland’s 2009 statute expressly rejects application of *Leegin*
  – *O’Brien v. Leegin Creative Leather Products* (Kansas 2012) – RPM agreements are *per se* unlawful under state law
    • Overruled by state legislature in 2013; RPM now subject to ROR
  – *People v. Tempur-Pedic International* (NY App. Div. 2012) – RPM agreements are *unenforceable* but not *unlawful* under state law
State Enforcement Attitudes

- 37 states supported per se rule in *Leegin* amicus brief
- 41 state attorneys general requested Congress to repeal *Leegin*
- Post-*Leegin* state minimum RPM prosecutions/consent decrees
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- Minimum RPM laws and State AG attitudes vary significantly by state
- Maximum RPM challenges are “mostly dead”
- National or multistate franchisors may face a challenge
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- Inquiry does not end with
  - Uncertain application of *Leegin’s* principles
  - Varying state statutes and court decisions
- Pre-*Leegin* tools remain available to help achieve uniformity in system pricing
Setting a Price Ceiling, not a Floor

Is maximum RPM absolutely safe?

• Disguised minimum RPM arrangement
• The California statutory caution
Unilateral Pricing Policy and Refusal to Deal with Violators

- *Colgate* doctrine – basic rule:
  - Supplier is free to deal, or refuse to deal, if done independently
    - *U.S. v. Colgate* (1919)
  - Supplier may unilaterally implement pricing policy
  - Devil is in details
Unilateral Pricing Policy and Refusal to Deal with Violators

• Joint v. unilateral action - reminder

• Colgate doctrine survives under Monsanto and Leegin

• Practical enforcement problems

• State non-antitrust law concerns
“Suggested” Resale Prices

• Permissible suggestion vs. coercion

• Range of permissible actions
  – Exposition, persuasion and argument
  – Providing suggested or list prices
  – Preticketing or advertising suggested prices
    • Curry v. Steve’s Franchise Co. (D. Mass. 1985)
    • Steak N Shake v. Globex Co. (D. Colo. 2015)
“Suggested” Resale Prices

• Coercive tactics may be unlawful
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• Any Colgate program must be truly unilateral
• Special circumstances may permit more mandatory compliance
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- If no “sale” of a product to a reseller, there remain no RPM issues
  - Genuine consignment arrangement: no transfer of control, title or risk of loss.
  - Supplier may properly set price at which commissioned sales agent must sell. *But see U.S. v. Apple, Inc. (2nd Cir. 2015)*
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- Suggested prices remain inviolate
- But manufacturers may pressure retailers to comply with nationally advertised price
  - *Jack Walters & Sons Corp v. Morton Building Inc.* (7th Cir. 1984)
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  – Worldhomecenter.com v. L.D. Kichler Co. (EDNY 2007)
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“Suggested” Resale Prices
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• Promotional pricing: required pass-through of supplier discounts to downstream retailers or consumers
  – *AAA Liquors v. Joseph E. Seagram & Sons* (10th Cir. 1982); *Jack Walters* (7th Cir. 1984)

• Temporary price reductions to meet competitive circumstances
  – *Sun Oil Co. v. FTC* (5th Cir. 1961)
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Questions / Discussion

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THE FALLOUT EIGHT YEARS AFTER LEEGIN: WHEN AND WHERE CAN FRANCHISORS FIX THE PRICES CHARGED BY FRANCHISEES?

I. BACKGROUND

On Memorial Day, 1977, nearly all "vertical restraints," i.e., "intrabrand" restrictions by suppliers or franchisors on sales by their own franchisees, dealers, or distributors, were automatically ("per se") illegal violations of Section 1 of the Sherman Act, 15 U.S.C. §1. No justification or other defense was permitted.

The *per se* rule, treating categories of restraints as necessarily illegal, eliminates the need to study the reasonableness of an individual restraint in light of the real market forces at work. The *per se* rule can give clear guidance for certain conduct. Restraints that are *per se* unlawful include horizontal agreements among competitors to fix prices or divide markets.

Resort to *per se* rules is confined to restraints, like those mentioned, "that would always or almost always tend to restrict competition and decrease output." To justify a *per se* prohibition, a restraint must have "manifestly anticompetitive" effects, and "lack ... any redeeming virtue." As a consequence, the *per se* rule is appropriate only after courts have had considerable experience with the type of restraint at issue.

In June, 1977, in *Continental TV, Inc. v. GTE Sylvania Inc.*, the Supreme Court overruled a 1967 Opinion and held that vertical restraints limiting the territory in which or the customers to whom the reseller could sell a given brand of goods were governed by the "Rule of Reason." Under the Rule of Reason, the supplier or franchisor may present evidence of the background, purpose, and justification for the restraint, including its pro-competitive effects in the relevant "interbrand" market, i.e., the market for all goods "reasonably interchangeable" with the product in question. "Under this rule, the factfinder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition." Appropriate factors to take into account include "specific information about the relevant business" and "the restraint's history, nature, and

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3 *Business Electronics, supra*, at 723.
9 *Id.* at 49.
effect.” Whether the businesses involved have market power is a further, significant consideration.

With almost no exceptions, a plaintiff cannot prevail in a Rule of Reason case absent proof that the intrabrand restraints had a significant adverse effect on competition in the overall interbrand market. In other words, absent a substantial interbrand market share, a supplier or franchisor has virtual carte blanche to impose vertical restraints on its resellers and franchisees. As the Court has held, the antitrust laws are concerned with “competition, not competitors.”

The trend toward applying the Rule of Reason to vertical restraints continued in 1984, when the Court held in Jefferson Parish Hospital Dist. No. 2 v. Hyde that “tying arrangements” were governed by the Rule of Reason (in the absence of a 30% or greater market share held by the franchisor). Resale price maintenance (“RPM”), however, remained a subject of special sensitivity, whose per se illegality continued for two decades after GTE Sylvania. The per se treatment of RPM derived from Dr. Miles Medical Co. v. John D. Park & Sons Co., a 1911 Supreme Court decision whose holding remained intact even as its conceptual underpinnings came into question. For example, in the same year as the Jefferson Parish tying decision, the Court declined to address the Solicitor General’s request to reconsider whether RPM should always be unlawful, but it did so only because neither party had raised that issue in the district court or on appeal. Four years later, the Court narrowed the scope of Dr. Miles, holding that per se illegality would apply when a supplier and dealers agree to set prices at some level, although perhaps not a specific level, but would not apply to an agreement solely to terminate a discounting dealer.

In 1997, the Court overruled in part a 1968 Opinion, and held that the Rule of Reason governed maximum resale price maintenance, i.e., the franchisor or supplier’s placing of a ceiling on resale prices. Minimum resale pricing, though, remained per se illegal for another full decade despite a history of increasing resistance to its general applicability to a variety of restrictive practices.

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10 State Oil Co. v. Khan, 522 U.S. 3, 100 (1997); Sylvania at 50.
15 220 U. S. 373 (1911).
20 See, e.g., Broadcast Music, Inc. v. Columbia Broadcasting System, Inc., 441 U. S. 1 (1979) (the per se rule is appropriate only when courts have had considerable experience with the type of restraint at issue); and Arizona v.
II. LEEGIN

In 2007 the final shoe dropped. Until then, as discussed more fully below, a franchisor could suggest minimum resale prices and use persuasion and exposition with its franchisees to convince them to charge those prices, but it was a *per se* violation for the franchisor to require (coerce) its franchisees to resell goods at a certain minimum price or price level, i.e., to refrain from discounting, assuming that was part of the supplier's overall program of RPM. But in *Leegin Creative Leather Products v. PSKS, Inc.*, the Court held that even a program to stamp out discount resale price competition was no longer *per se* illegal – it, too, is governed by the Rule of Reason.

Thirty-seven states filed an unsuccessful amicus brief in *Leegin*, arguing for continuing the *per se* rule. And crucially, as described below, states do not uniformly follow *Leegin*. Hence, even though Congressional efforts to override *Leegin* have gotten nowhere, and no Congressional action is remotely likely, at present a franchisor which imposes *nationwide* minimum resale prices still has major concerns.

A. Facts / Background

The facts in *Leegin* were these: Plaintiff PSKS operated a women's apparel store in Texas. Its signature brand of leather goods and accessories was the "Brighton" line, produced by the defendant. The defendant began a policy of refusing to sell to retailers which discounted Brighton products below its suggested prices, presenting the policy as encouraging the more than 5,000 boutiques that were the main Brighton outlets to offer their customers a higher-quality sales and service experience than the "mega stores" offered.

When PSKS refused the defendant's request that it stop discounting the Brighton line, the defendant stopped supplying PSKS, whose revenue declined. PSKS sued, alleging that the defendant had entered into unlawful resale price-fixing agreements with its retailers. At trial, *Leegin* asserted that its program was unilateral and lawful. The court did not allow *Leegin* to introduce expert testimony on the procompetitive benefits of its pricing policy, ruling that the testimony was irrelevant under the *per se* rule. The jury found for PSKS, and the court entered judgment of nearly $4 million in treble damages, attorneys' fees and costs.

On appeal, *Leegin* did not contest the finding that it had entered into RPM agreements with its dealers. Instead, it asserted that the law should be changed, and the Rule of Reason rather than the *per se* rule should have been applied. The Fifth Circuit, recognizing that it remained bound by prior precedent, affirmed.

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*Maricopa County Medical Soc.*, 457 U. S. 332 (1982) (*per se* treatment should be applied to a practice only if courts can predict with confidence that it would be invalidated in all or almost all instances under the Rule of Reason).


B. Supreme Court Decision

The Supreme Court reversed, concluding 5-4 that the per se rule should be jettisoned and these restraints, like all other vertical restraints, should be judged under the Rule of Reason. It overruled 96 years of precedent, starting with the venerable Dr. Miles decision.24

The majority opinion rested on three main propositions. First, it found that "[t]he reasoning of the Court's more recent jurisprudence has rejected the rationales on which Dr. Miles was based,"25 One of those rationales—the common-law rule against restraints on alienation—now seemed an anachronistic formalism rather than a justification resting on "demonstrable economic effect."26 The other rationale of Dr. Miles—that the vertical arrangements were analogous to a horizontal agreement among competing dealers—was also outdated: "Our recent cases formulate antitrust principles in accordance with the appreciated differences in economic effect between vertical and horizontal agreements, differences the Dr. Miles court failed to consider."27

Second, reconsidering the matter, the majority found that a per se rule was not justified because, although "the potential anticompetitive consequences of vertical price restraints must not be ignored or underestimated,"28 vertical agreements setting minimum resale prices can have procompetitive justifications.29 Finally, the court determined that, given the serious "flaws of Dr. Miles in light of modern antitrust jurisprudence," considerations of stare decisis did not mandate retaining it. The Court noted that "[o]nly eight years after Dr. Miles ... the Court reined in the decision by holding [in United States v. Colgate & Co.30] that a manufacturer can announce suggested resale prices and refuse to deal with distributors who do not follow them."31

C. Competitive Considerations

The Supreme Court had previously recognized that RPM may be procompetitive, but Leegin took that recognition even further. In State Oil Co. v. Khan, the Court noted that, where there is vigorous competition, a per se rule against vertical maximum price fixing could actually be harmful to competition and consumers' welfare.32 In Leegin, the Court offered several possible procompetitive justifications that may be applicable to minimum RPM, including the following:

24 220 U.S. 73 (1911).
25 Leegin, 551 U.S. at 887.
26 Id. at 887-888 (quoting Sylvania).
27 Id. at 888.
28 Id. at 894.
29 Id. at 892.
30 250 U.S. 300 (1919).
31 Id. at 901.
32 Khan, 522 U.S. at 18.
• By tending to eliminate intrabrand price competition, RPM “encourages retailers to invest in tangible or intangible services or promotional efforts that aid the manufacturer’s position as against rival manufacturers.”

• RPM may also “give consumers more options so that they can choose among low-price, low-service brands; high-price, high-service brands; and brands that fall in between.”

• Without RPM, “retail services that enhance interbrand competition might be underprovided” because of the risk of free riding by discounting retailers who do not invest in the facilities and services provided by higher service, higher price retailers.

• Market entry by new firms and brands may be facilitated by RPM, which could encourage “competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer.”

The Court also acknowledged, though, that minimum RPM could have anticompetitive effects, including facilitating manufacturer or retailer cartels, discouraging price reductions for the benefit of consumers, forestalling distribution innovations that might reduce costs and incentivizing retailers not to sell the products of rival manufacturers. In order to determine whether RPM is anticompetitive in any particular case, the Court said that various factors would have to be weighed, including the following:

• The number of manufacturers in a given industry that have adopted RPM practices. “When only a few manufacturers lacking market power adopt the practice, there is little likelihood it is facilitating a manufacturer cartel, for a cartel can then be undercut by rival manufacturers…. [RPM] should be subject to more careful scrutiny, by contrast, if many competing manufacturers adopt the practice.”

• Whether the impetus for RPM is the manufacturer or its retailers. “If there is evidence that retailers were the impetus for a vertical price restraint, there is a greater likelihood that the restraint facilitates a retailer cartel or supports a dominant, inefficient retailer.”

33 Leegin, 551 U.S. at 890.
34 Id.
35 Id. at 890-891.
36 Id. at 891, quoting Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 55 (1977)
37 Id. at 892-894.
38 Id. at 897.
39 Id. at 897-898.
• Whether the manufacturer or retailers possess market power. “If a retailer lacks market power, manufacturers likely can sell their goods through rival retailers…. And if a manufacturer lacks market power, there is less likelihood it can use the practice to keep competitors away from distribution outlets.”

D. Assessment of Decision

_Leevin_ was not the blanket endorsement of minimum RPM one might assume in an initial reading. As noted above, the Court pointed out that evidence of illegality under the Rule of Reason might include (i) a market characterized by suppliers all or nearly all of whom imposed such a minimum price restraint on franchisees, (ii) where the franchisor had market power, notably a large market share, providing it the ability to raise prices or exclude interbrand competition (the classic Rule of Reason test), or (iii) where the restraint was agreed upon by franchisees themselves (horizontally), and in effect was foisted upon the franchisor by a franchisee cartel.

Although the _Leevin_ decision would appear on its face to liberalize the law affecting minimum RPM practices, it has been dismissed by one commentator as “a Pyrrhic victory, increasing both litigation and liability risks even for the well-counseled defendant-seller, since fewer cases will be dismissed at early stages, many more will go to trial, and plaintiffs will likely win their share.” Indeed, the Court in _Leevin_ gave little guidance to the lower courts as to how they should apply the factors discussed in the Court’s opinion. Rather, the Court left it to subsequent decisions as to how those factors should be addressed, stating:

“As courts gain experience considering the effects of [RPM] restraints by applying the rule of reason over the course of decisions, they can establish the litigation structure to ensure the rule [of reason] operates to eliminate anticompetitive restraints from the market and to provide more guidance to businesses. Courts can, for example, devise rules over time for offering proof, or even presumptions where justified, to make the rule of reason a fair and efficient way to prohibit anticompetitive restraints and to promote procompetitive ones.”

The dissenters, in an opinion by Justice Breyer joined by Justices Stevens, Souter and Ginsburg, framed the issue as "whether to change a clear and simple price-related antitrust rule that the courts have applied for nearly a century." They could point to no new circumstances that would justify "abandoning a well-established antitrust rule."

40 _Id._ At 898.

41 _Id._ at 892-94.


43 _Leevin_, 551 U.S. at 898-899.

44 _Id._ at 918 (Breyer, J., dissenting).

45 _Id._ at 923. From the perspective of academe, it is too early to determine the economic results of _Leevin_, but one respected study concluded in 2014 as follows:

Our results indicate that prices and quantities have indeed changed as a result of _Leevin_. We find that 8.4 percent of products exhibited a statistically significant price increase in our treatment states, with
While the dissenters found *Dr. Miles* per se rule "clear and simple," they lamented that the *Leequin* majority's Rule of Reason test for minimum RPM was not. Noting that "it is now unknown ... how courts will decide future cases under a 'Rule of Reason,'" the dissent predicted that the majority's change of the legal standard "will unsettle the law," and "will create considerable legal turbulence as lower courts seek to develop workable principles."

III. FEDERAL COURT RESPONSES TO LEEQUIN

While beneficial to franchisors and other suppliers that wish to stamp out discounting by their franchisees and reseller customers, *Leequin* has not resulted in uniform franchisor victories in lower courts. Thus, in *Toledo Mack Truck Sales & Service v. Mack Trucks, Inc.*, the minimum RPM claims survived, despite a complete Rule of Reason evaluation. The Third Circuit reversed the trial court and ruled the plaintiff had presented sufficient evidence that Mack Truck dealers first had colluded horizontally to enter into "gentlemen's agreements" not to compete with each other, and Mack Trucks agreed vertically as a result to deny or delay sales assistance to any dealer selling outside its area of responsibility, thus preventing dealer competition. Mack's Achilles' heel was that its restraints resulted from a dealer cartel's pressure, not its own independent decision, one of the evidentiary factors identified in *Leequin* as a sign of illegality.

In another case, the "dominant retailer" factor in *Leequin* led to the Court's upholding plaintiff's Rule of Reason analysis in a suit by retailers and consumers against Toys "R" Us, alleging the defendant used its very strong market position to coerce manufacturers to force minimum RPM on their retailers who competed with Toys "R" Us. Denying a motion to dismiss, the Court held plaintiffs had adequately pled antitrust injury although the alleged competitive harm was intrabrand; this was because the "dominant retailer" imposed the restraint, which substantially impacted interbrand competition as a whole. And in *McDonough v. Toys "R" Us, Inc.*, the court certified a class of consumers who alleged they were overcharged a median increase of 5.3 percent. Additionally, 9.4 percent of products experienced declining quantities. As a result of *Leequin*, products were most likely to see a price increase combined with a quantity decrease. This combination indicates movement along the demand curve and suggests the exercise of market power. We estimate an overall price increase of 0.33 percent and an overall quantity decrease of 3.8 percent.

Firms may still be held liable for anticompetitive behavior resulting from RPM contracts. Because of this, they may not be acting as anticompetitively as they might if RPM were per se legal. Still, whether through undetected anti-competitive behavior or unsuccessful retailer service strategies, a simple welfare analysis of the rule-of-reason environment shows that the harm to consumers [under *Leequin*] outweighs the benefits.


46 Id. at 926.
47 Id. at 924.
48 Id. at 929.
49 530 F.3d 204 (3d Cir. 2008).
when they purchased certain baby products because the defendant retailer "coerced [baby products] manufacturers into adopting vertical price restraints—policies designed to prevent retail discounting—that would insulate [the defendant] from price competition." The court determined that the putative class could prove the essential elements of its minimum RPM claims under the rule of reason without resort to individualized proof (as required by Rule 23(b)(3)). In doing so, the court pointed to the suggestion in *Leegin* that "[i]f there is evidence [that] retailers were the impetus for a vertical price restraint, there is greater likelihood that the restraint ... supports a dominant, inefficient retailer." The court found that the class had "offered evidence that [the defendant] was a dominant retailer that coerced vertical restraints to prevent internet discounting," and that "[n]othing in this argument require[d] evidence that would be individual to subclass members."

In 2015, major discount retailer COSTCO launched an attack on Johnson & Johnson Vision Care, Inc. ("J&J"), alleging J&J is "the dominant company in a unique marketplace" of sales of contact lenses. COSTCO alleged J&J, under pressure from some of its customers—eye care professionals who sell contact lenses in competition with COSTCO and other J&J customers which discount resales—agreed to limit competition by discounters by requiring certain minimum retail prices. COSTCO complained, but complied with the restraint to avoid loss of supply. Now it has sued. This case raises Rule of Reason issues under *Leegin*, as well as the claim of a concerted refusal to deal, invoking the so-called *Monsanto* doctrine, derived from *Monsanto Co. v. Spray-Rite Service Corp.*

On the other hand, *Leegin* has led to numerous defense victories. In *Columbus Drywall & Insulation, Inc. v. Masco Corp.*, the court granted summary judgment against vertical price-fixing claims asserted by a class of independent fiberglass insulation contractors against the defendant, a competing fiberglass insulation contractor, and four of the leading fiberglass insulation manufacturers in the United States. The plaintiffs claimed that the manufacturers agreed to maintain a "spread" between the prices they charged the defendant and the prices they charged plaintiffs, in exchange for which the defendant agreed to support an industry-wide price increase for insulation. The court observed that there was evidence that "[the defendant]
entered into a series of vertical agreements concerning the [alleged] spread,"61 and that those agreements had led plaintiffs to pay increased prices for insulation.62 But, absent proof of a horizontal agreement among manufacturers, the Court held that the rule of reason applied and that the plaintiffs had failed to present sufficient evidence that the alleged agreements had an anticompetitive effect.63 The court rejected the plaintiffs' argument that the "combined effects of the vertical agreements"—as opposed to the effects of "any one of the individual [vertical] conspiracies" sufficed to show an adverse effect on competition, reasoning that the effects of the vertical agreements could not be aggregated "in the absence of an agreement between or concerted action by the manufacturers."64

Similarly, the court in Jacobs v. Tempur-Pedic Intl., Inc.65 dismissed a consumer class action, holding Tempur-Pedic's minimum RPM agreements with distributors were protected under Leegin, where the plaintiffs did not plead sufficient facts to show an anticompetitive effect in the relevant interbrand market.

Plaintiff, who had purchased a Tempur-Pedic mattress from a Tempur-Pedic distributor at a price equal to or exceeding the minimum retail price stated in the distributor's agreement with Tempur-Pedic (Tempur-Pedic set the minimum retail prices its distributors could charge for mattresses), claimed that Tempur-Pedic violated the Sherman Act both by enforcing RPM agreements downstream upon its buyer-distributors, and by engaging in horizontal price-fixing with its distributors, who were also its competitors, because Tempur-Pedic also had company store sales. Plaintiff sought treble damages on behalf of all United States purchasers of Tempur-Pedic mattresses and an injunction against Tempur-Pedic's RPM agreements. The district court dismissed plaintiff's complaint for failure to state a claim for relief and the Eleventh Circuit Court of Appeals affirmed the dismissal.

Reviewing plaintiff's claims de novo, the Court set out to determine whether the complaint "possessed enough heft to show that the pleader is entitled to relief."66 The allegations had to nudge the claim "across the line from conceivable to plausible," meaning that the complaint needed "more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do."67 The Court summarily traced the evolution of vertical restraints under the Sherman Act, noting that, "by the time the (Supreme) Court decided Leegin, the jurisprudential foundations supporting the analysis of vertical resale price minimums under the per se rule were already substantially weakened."68 After Leegin, therefore, courts had to evaluate vertical resale price restraints under the rule of reason rather than the per se rule.

61 Id. at *53.
62 Id.
63 Id. at *53-55.
64 Id. at *55-57 (citing Dickson v. Microsoft Corp., 309 F.3d 193,203-204 (4th Cir. 2002), and PepsiCo, Inc. v. Coca-Cola Co., 315 F.3d 101, 109-10 (2d Cir. 2002)).
65 626 F.3d 1327 (11th Cir. 2011).
66 Id. at 1332-33 (quotations and alteration omitted).
67 Id. at 1333 (citations omitted).
68 Id. at 1335.
To prove a Rule of Reason violation, plaintiff first had to identify the relevant market (comprised of both product and geographic components) in which the alleged competitive harm occurred or would occur. However, plaintiff’s deficient relevant market allegations alone doomed its complaint. Plaintiff claimed that Tempur-Pedic visco-elastic foam mattresses should have been considered a distinct product submarket and not part of one larger market for all mattresses, as the district court had concluded. The Eleventh Circuit, though, felt that plaintiff’s “skimpy allegations of the relevant submarket” did not plausibly suggest the relevant submarket’s composition. “The complaint provide[d] no factual allegations of the cross-elasticity of demand or other indications of price sensitivity that would indicate whether consumers treat visco-elastic foam mattresses differently than they do mattresses in general. Consumer preferences for visco-elastic foam mattresses versus traditional innerspring mattresses, and the costs associated with their sale, may vary widely, may vary little, or may not vary at all.”

Consequently, plaintiff’s allegations were legally insufficient.

In any event, plaintiff failed adequately to allege actual or potential harm to competition. Actual anticompetitive effects included output reduction, price increases or deterioration in quality. Consumer welfare, understood in the sense of allocative efficiency, is the animating concern of the Sherman Act. Yet plaintiff simply stated baldly that consumers lost hundreds of millions of dollars; it did not assert the competitive level above which Tempur-Pedic’s allegedly anticompetitive conduct artificially raised prices. Nor did it adequately allege potential competitive harm. Plaintiff’s complaint was "bereft of the critical allegations linking [Tempur-Pedic’s] market power [in the visco-elastic foam mattress market, even if that was the properly defined market] to harm to competition."

The Eleventh Circuit likewise upheld the district court’s dismissal of plaintiffs’ horizontal price fixing claim, which was based on Tempur-Pedic’s dual distribution structure selling mattresses through distributors and its own website. Plaintiff had the burden to allege "why it is more plausible that [Tempur-Pedic] and its distributors—assuming they are rational actors acting in their economic self-interest—would enter into an illegal price-fixing agreement (with the attendant costs of defending against the resulting investigation) to reach the same result realized by purely rational profit maximizing behavior." However, the complaint lacked facts plausibly suggesting a conspiracy when the "inference of conspiracy is juxtaposed with the inference of independent self-interest.”

Another post-Leegin case, reminiscent of a case almost 90 years ago concerning RPM, analyzed whether the "agency defense" to vertical price fixing remains available to suppliers. In Valuepest.Com of Charlotte, Inc. v. Bayer Corp., three distributors brought a class action suit alleging that Bayer and BASF violated Section 1 of the Sherman Act by

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69 Id. at 1338.
70 Id. at 1339 (citations omitted).
71 Id. at 1340.
72 Id. at 1342.
73 Id. at 1343.
75 561 F.3d 282 (4th Cir. 2009).
engaging in vertical price fixing. Plaintiffs’ allegations stemmed from defendants' non-exclusive agency agreements, whereby Univar USA, a distributor-agent, received commissions in exchange for facilitating sales of defendants' termiticides. Under the arrangements, the distributor received a fixed commission and defendants retained ownership and the ability to set the retail price of the product. Plaintiffs claimed that the arrangement was a sham transaction designed to allow prohibited resale price maintenance, a practice in which a manufacturer and distributor agreed on a minimum price, below which the distributor would not sell the product.

After staying the case pending the Supreme Court's decision in *Leegin*, the district court granted summary judgment for defendants, holding that defendants' contracts with their distributor represented genuine agency relationships that did not support liability under Section 1 of the Sherman Act. Plaintiffs appealed, claiming that *Leegin* rendered the agency defense no longer viable or, alternatively, that the defendants' contracts with their distributor were sham agreements rather than true agency relationships.

The district court's analysis began by rejecting plaintiffs' claim that *Leegin* overturned the agency defense to claims of resale price maintenance. The court then considered and rejected plaintiffs' contention that the agency agreement was a sham. The court began its analysis of the agreement by noting it must look to the substance rather than the form of the parties' dealings, and that the most important factor was how business risks were allocated between the parties. Where distributors deal with suppliers as independent businessmen who bear most of the risks of transactions with purchasers, the agency defense does not protect the manufacturer. However, where the manufacturer bears the financial risks of the transactions with customers, the distributor is likely an agent. The court also noted that an inquiry into the genuineness of an agency agreement required the court to consider the economic justification for the agreement and whether or not the agreement was a product of coercion.76

Finally, on remand, Leegin itself successfully defended the suits against it under the Rule of Reason.77 These developments have taken place against the backdrop of the heightened pleading standard imposed on complaints by *Bell Atl. Corp. v. Twombly*78 and *Ashcroft v. Iqbal*,79 suggesting that franchisees will continue to face difficulties in pleading all of the elements required for a successful Rule of Reason claim against a franchisor's RPM program.80

IV. THE STATES: THE CRUCIAL ARENA

RPM prohibitions in state statutes are not preempted by the Sherman Act.81 Thus the antitrust laws of 50 individual states, the District of Columbia, Puerto Rico and the Virgin Islands

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76 561 F.3d at 291.
77 *PSKS, Inc. v. Leegin*, 615 F. 3d 412 (5th Cir. 2010) (which also rejected the claim that where the supplier engages in dual distribution, having both franchises and retail operations, that makes the restraints it imposes "horizontal"; holding dual distribution is analyzed as a vertical practice under the Rule of Reason).
80 *Cf., e.g., Rick-Mik Enterprises v. Equilon Enterprises*, 532 F.3d 963 (9th Cir. 2008)
81 See *California v. ARC America Corp.*, 490 U.S. 93 (1989).
are also applicable to RPM practices in the United States. While Khan and Leegin may be persuasive as to how those laws should be interpreted, neither has any direct effect on those laws. In some cases state laws may produce an outcome quite different than what would result under federal law. The resulting patchwork quilt of differential treatment of RPM practices can be perplexing for a franchisor or supplier seeking to establish a uniform national set of product pricing practices.

Nineteen states, by statute or court ruling, at least arguably do or may prohibit minimum RPM on a per se basis. Those states include the following:

- California, whose statute broadly prohibits “trusts” and also expressly addresses RPM practices;
- Connecticut, which declares illegal contracts, combinations or conspiracies with the purpose or effect of price fixing;
- Hawaii, whose statute prohibits a number of practices, including refusals to deal, which have the purpose or effect of fixing prices;
- Illinois, which makes unlawful price fixing as well as production or supply limitations whose effect is to fix prices.

82 For a state-by-state analysis of RPM laws, see Michael A. Lindsay, Chart, Overview of State RPM, Supplement to THE ANTITRUST SOURCE (Oct. 2014), http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/lindsay_chart.authcheckdam.pdf.

83 CAL. BUS. & PROF. CODE § 16720(d) (defining a prohibited “trust” as “a combination of capital, skill or acts by two or more persons … [t]o limit or reduce the production, or increase the price of merchandise or of any commodity … [t]o fix at any standard or figure, whereby its price to the public or consumer shall be in any manner controlled or established, … not to sell, dispose of or transport any article or any commodity or any article of trade, use, merchandise, commerce or consumption below a common standard figure, or fixed value … to keep the price of such article, commodity or transportation at a fixed or graduated figure [or] [e]stablish or settle the price of any article, commodity or transportation between them or themselves and others, so as directly or indirectly to preclude a free and unrestricted competition among themselves, or any purchasers or consumers in the sale or transportation of any such article or commodity”). See also text accompanying notes 117 – 124 infra.

84 CONN. GEN. STAT. ANN. § 35-28 (declaring unlawful “every contract, combination, or conspiracy …when the same are for the purpose, or have the effect, of …[f]ixing, controlling, or maintaining prices, rates, quotations, or fees in any part of trade or commerce”). But see Navien American, Inc. v. Allen, 2011 WL 3925729 (Conn. Super. Ct. 2011) (In granting a motion to strike a price-fixing counterclaim in a collection action, the Superior Court observed, “Notwithstanding Connecticut's historic position for the maintenance of the per se test, this court has not been provided with any Connecticut antitrust statutes or pertinent state law to permit it not to follow Leegin as a federal precedent. The court finds that the rule of reason analysis is the applicable standard in this case to determine if there has been a violation of the Connecticut Antitrust Act”).

85 HAW. REV. STAT. § 480-4(b) (prohibiting “any understanding, arrangement, pool, or trust, to …, directly or indirectly, (1) [f]ix, control, or maintain, the price of any commodity; … (3) [f]ix, control, or maintain, any standard of quality of any commodity for the purpose or with the result of fixing, controlling, or maintaining its price; [or] (4) [r]efuse to deal with any other person or persons for the purpose of effecting any of the acts described” above).

86 ILL. COMP. STAT. ANN. 10/3(1)(A) (making unlawful any contract, combination or conspiracy with “any other person who is, or but for a prior agreement would be, a competitor … for the purpose or with the effect of fixing, controlling, or maintaining the price or rate charged for any commodity sold or bought by the parties thereto, or the fee charged or paid for any service performed or received by the parties thereto; [or] … fixing, controlling, maintaining, limiting, or discontinuing the production, manufacture, mining, sale or supply of any commodity, or the sale or supply of any service, for the purpose or with the effect stated” above). But see House of Brides, Inc. v. Alfred Angelo, Inc., No. 11 C 07834, 2014 WL 64657 (N.D. Ill. Jan. 8, 2014)(applying Rule of Reason analysis to a federal vertical RPM claim and similar treatment, with scant analysis, to an accompanying claim under the state statute). Compare New York v. Herman Miller, Inc., 2008-2 Trade Cas. (CCH) ¶ 76,454 (S.D.N.Y. Mar. 25, 2008), discussed in text accompanying note 114 infra.
• Indiana, with a straightforward prohibition of price fixing; 87
• Kansas, whose statutory per se treatment of RPM has been the subject of significant judicial and legislative attention; 88
• Louisiana, whose statute generically prohibits agreements in restraint of trade; 89
• Maryland, which declares minimum price restrictions illegal; 90
• Minnesota, which declares price fixing, as well as production and supply limitations having the effect of price fixing, to be unreasonable restraints of trade; 91
• Mississippi, whose statute on its face prohibits maximum as well as minimum RPM; 92
• Montana, which makes unlawful agreements to fix or control prices; 93
• Nebraska, whose statute does not expressly deal with price fixing but has been interpreted as treating RPM as a per se violation; 94

87 IND. CODE ANN. § 24-1-2-1 (making illegal “[e]very scheme, contract, or combination to … limit or reduce the production, or increase or reduce the price of merchandise or any commodity”).

88 KAN. STAT. ANN. § 50-101 (declaring unlawful as a trust any “combination of capital, skill, or acts, by two or more persons,” to do one of several things, including “[t]o fix any standard or figure, whereby such person’s price to the public shall be, in any manner, controlled or established, any article or commodity of merchandise, produce or commerce intended for sale, use or consumption in this state”); and KAN. STAT. ANN. § 50-112 (declaring unlawful “all arrangements, contracts, agreements, trusts, or combinations between persons made with a view or which tend to … advance, reduce or control the price or the cost to the producer or to the consumer of any such products or articles”). But see text accompanying notes 102 – 105 infra.

89 LA. REV. STAT. ANN. §51:122 (making unlawful “[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce”). While commentators predict that Louisiana would follow federal precedent in analyzing RPM practices, see 1 STATE ANTITRUST PRACTICE AND STATUTES at Louisiana 21-1 (2009), there is one dated prior decision stating in dictum that “Vertical price restrictions are per se illegal.” Red Diamond Supply Inc. v. Liquid Carbonic Corp., 637 F.2d 1001, 1005 n.6 (5th Cir. 1981).

90 MD. CODE ANN. COM. LAW § 11-204 (defining as “an unreasonable restraint of trade or commerce” any “contract, combination, or conspiracy that establishes a minimum price below which a retailer, wholesaler, or distributor may not sell a commodity or service”). See also text accompanying notes 106 – 111 infra.

91 MINN. STAT. ANN. § 325D.53 Subdiv. 1 (declaring as an unreasonable restraint of trade and unlawful any “contract, combination, or conspiracy … for the purpose or with the effect of affecting, fixing, controlling or maintaining the market price, rate, or fee of any commodity or service or … affecting, fixing, controlling, maintaining, limiting, or discontinuing the production, manufacture, mining, sale or supply of any commodity, or the sale or supply of any service, for the purpose or with the effect of affecting, fixing, controlling, or maintaining the market price, rate, or fee of the commodity or service”). See also State v. Alpine Air Prods., Inc., 490 N.W.2d 888 (Minn. Ct. App. 1992), in which the court observed that “Minnesota courts have consistently held that Minnesota antitrust law is to be interpreted consistently with the federal courts’ construction of federal antitrust law” but also noted that “[p]er se violations of Minnesota antitrust laws are enumerated in Minn.Stat. § 325D.53,” and therefore held that a vertical minimum price fixing agreement was a per se violation of Minnesota law.

92 MISS. CODE ANN. § 75-21-1(b) (defining as an unlawful trust or combine any “combination, contract, understanding or agreement, expressed or implied,” whose effect would be “[t]o limit, increase or reduce the price of a commodity”).

93 MONT. CODE ANN. § 30-14-205 (declaring it unlawful for one or more persons directly or indirectly “to enter into an agreement for the purpose of fixing the price or regulating the production of an article of commerce” or to “fix a standard or figure whereby the price of an article of commerce intended for sale, use, or consumption will be in any way controlled”).

94 NEB. REV. STAT. § 59-801 (declaring illegal “[e]very contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce”). In a pre-Leegin decision, the Nebraska Supreme Court declared that “[b]oth horizontal price-fixing among wholesalers and vertical price-fixing between wholesalers and retailers are
• Nevada, which prohibits price fixing in several different formulations; 95
• New Hampshire, which makes unlawful price or rate fixing; 96
• New Jersey, which prohibits minimum RPM restraints; 97
• New York, whose statute states that minimum RPM provisions “shall not be enforceable or actionable”; 98
• Ohio, which prohibits price fixing and other resale price limitations; 99
• South Carolina, which makes unlawful all forms of price fixing; 100 and
• West Virginia, which prohibits RPM and related practices. 101

Since Leegin, state RPM laws have been the subject of significant litigation, government enforcement actions and legislation. The experience in several of these states is instructive.

In Kansas, the state Supreme Court held in 2012 that, even after Leegin, RPM agreements would be considered per se unlawful under the Kansas antitrust law. 102 That decision, however, was effectively reversed by the Kansas legislature which, on April 16, 2013,

presumed to be in restraint of trade and are per se violations of the antitrust laws.” State ex rel. Douglas v. Associated Grocers, 214 Neb. 79, 332 N.W.2d 690 (Neb. 1983), in which the court cited federal precedent for the proposition that “horizontal price-fixing among wholesalers and vertical price-fixing between wholesalers and retailers are presumed to be in restraint of trade and are per se violations of the antitrust laws.”

95 NEV. REV. STAT. ANN. § 598A.060 (prohibiting “[p]rice fixing, which consists of raising, depressing, fixing, pegging or stabilizing the price of any commodity or service”).

96 N.H. REV. STAT. ANN. § 356:2 (declaring unlawful “[e]very contract, combination, or conspiracy … which has the purpose or the effect of … [f]ixing, controlling or maintaining prices, rates, quotations or fees in any part of trade or commerce”).

97 N.J. STAT. § 56:4-1.1 (“Any contract provision that purports to restrain a vendee of a commodity from reselling such commodity at less than the price stipulated by the vendor or producer shall not be enforceable or actionable at law”). See also Exit A Plus Realty v. Zuniga, 395 NJ Super. 655, 930 A. 2d 491 (N.J. Super. Ct. App. Div. 2007), in which a post-Leegin decision confirms that the state statute renders vertical RPM arrangements per se unenforceable but fails to mention Leegin itself).

98 N.Y. GEN. BUS. LAW § 369-a (“Any contract provision that purports to restrain a vendee of a commodity from reselling such commodity at less than the price stipulated by the vendor or producer shall not be enforceable or actionable at law”). See also text accompanying notes 65 – 73 supra and 116 infra.

99 OHIO REV. CODE ANN. § 1331.01(B)(4) (declaring unlawful any trust whose purpose is “[t]o fix at a standard or figure, whereby its price to the public or consumer is in any manner controlled or established, an article or commodity of merchandise, produce, or commerce intended for sale, barter, use or consumption”); OHIO REV. CODE ANN. § 1331.02 (prohibiting any person from entering into a combination, contract or agreement “with the intent to limit or fix the price … of an article or service of commerce, use, or consumption”). See also Ohio ex. rel. Brown v. Andrew Palzes, Inc., 39 Ohio Misc. 155, 317 N.E.2d 262 (Ohio Com. Pl. 1973), stating that “[p]rice-fixing is a per se violation under the antitrust statutes of this state” and holding that a maximum resale price agreement violated § 1331.01(B).

100 S.C. CODE ANN. § 39-3-10 (declaring unlawful “[a]ll arrangements, contracts, agreements, trusts or combinations … designed or which tend to advance, reduce or control the price or the cost to the producer or consumer of any such product or article”).

101 W. VA. CODE ANN. § 47-18-3 (declaring unlawful every “contract, combination or conspiracy … for the purpose or with the effect of fixing, controlling, or maintaining the market price, rate or fee of any commodity or service; or … fixing, controlling, maintaining, limiting or discontinuing the production, manufacture, mining, sale or supply of any commodity, or the sale or supply of any service, for the purpose or with the effect of fixing, controlling or maintaining the market price, rate or fee of the commodity or service”).

enacted a statute that specified Rule of Reason treatment for RPM agreements. The amended restraint of trade statute expressly instructs that “the Kansas … act shall be construed in harmony with ruling judicial interpretations of federal antitrust law by the United States supreme court” and then goes on to mandate Rule of Reason treatment in the following terms:

An arrangement, contract, agreement, trust, understanding or combination shall not be deemed a trust pursuant to the Kansas restraint of trade act and shall not be deemed unlawful, void, prohibited or wrongful under any provision of the Kansas restraint of trade act if that arrangement, contract, agreement, trust, understanding or combination is a reasonable restraint of trade or commerce. An arrangement, contract, agreement, trust, understanding or combination is a reasonable restraint of trade or commerce if such restraint is reasonable in view of all of the facts and circumstances of the particular case and does not contravene public welfare.

The experience in Maryland has been quite different. There a post-Leegin 2009 state statute not only prohibits minimum RPM but criminalizes it. The statute, which amended a provision of the state Commercial Law, provides that “a contract, combination, or conspiracy that establishes a minimum price below which a retailer, wholesaler, or distributor may not sell a commodity or service is an unreasonable restraint of trade or commerce.” Violations of the statute may be pursued civilly or in criminal proceedings. While the import of this law may seem obvious, the Deputy Chief of the Antitrust Division of the Maryland Attorney General’s Office has confirmed that the 2009 amendment, which he characterizes as a “Leegin Repealer,” was expressly intended to reject Leegin and restore the per se rule for RPM agreements in his state.

The general enforcement mood with respect to RPM at the state level is one of hostility, as reflected both by the 37 states which argued in Leegin for retention of the per se rule and by the 41 state attorneys general who, in a 2009 letter sent to Congress, requested that the

104 KAN. STAT. ANN. § 50-163(b).
105 Id. § 50-163(c).
107 MD. CODE ANN. COM. LAW § 11-204.
108 Id. § 11-204(b).
109 Id. § 11-209.
110 Id. § 11-207.
Leegin holding be statutorily overruled.\textsuperscript{113} That generalized hostility has manifested itself in several state minimum RPM prosecutions after Leegin. New York, Michigan, Illinois and California have all alleged \textit{per se} treatment and entered into consent decrees on that basis,\textsuperscript{114} and \textit{per se} treatment has found traction in civil litigation as well.\textsuperscript{115} New York's long litigation with Tempur-Pedic led to an anomalous finding that the New York antitrust law renders minimum RPM agreements "unenforceable" but not illegal.\textsuperscript{116}

California has been among the most consistent and persistent of the states in pursuing minimum RPM arrangements as \textit{per se} violations of the state statute. The state's modern-day RPM case law traces back to \textit{Mailand v. Burckle},\textsuperscript{117} a California Supreme Court decision which declared that price fixing, whether of a horizontal or vertical nature, is a \textit{per se} violation of state antitrust law. The court observed that it is irrelevant whether "prices set pursuant to a price-fixing scheme are reasonable, for the 'reasonable price fixed today may through economic and business changes become the unreasonable price of tomorrow.'"\textsuperscript{118} The court also noted that the state Cartwright Act had been interpreted "to prohibit tampering with prices; they must be determined, we have stated, by the 'interplay of the economic forces of supply and demand.'"\textsuperscript{119}

The \textit{Mailand v. Burckle} opinion also stated that "[s]ince the Cartwright Act is patterned after the Sherman Act (15 U.S.C. § 1 et seq.), federal cases interpreting the Sherman Act are applicable in construing our state laws."\textsuperscript{120} Notwithstanding that concept, the decision's \textit{per se} treatment of RPM practices has continued in effect even after Leegin.\textsuperscript{121} In the most recent decision addressing the issue, \textit{Alsheikh v. Superior Court},\textsuperscript{122} an unpublished intermediate appellate court opinion, the court granted a writ of mandate and remanded the case to the trial court with instructions to sustain a demurrer against the plaintiff's RPM allegations because the


\textsuperscript{115} See, e.g., \textit{Darush MD APC v. Revision LP}, No. 12-cv-10296 (C.D. Cal. July 16, 2013) (finding parties' communications were sufficient under \textit{per se} rule to make plausible an agreement to "vertically fix prices and eliminate retailers selling at a discount"); \textit{Alsheikh v. Superior Court}, No. B249822, 2013 WL 5530508 (Cal. App. 2d Dist. Oct. 7, 2013), review denied (Jan. 15, 2014) (noting in remand that "if there were vertical price fixing, that would . . . be a \textit{per se} violation under the California statute.


\textsuperscript{117} 20 Cal.3d 367 (1978).

\textsuperscript{118} \textit{Id.} at 377 (citing \textit{United States v. Trenton Potteries} 273 U.S. 392 (1927)).

\textsuperscript{119} \textit{Id.} (citing \textit{Speegle v. Board of Fire Underwriters}, 29 Cal.2d 34 (1946)).

\textsuperscript{120} \textit{Id.} at 376.

\textsuperscript{121} See, e.g., cases cited at notes 114 – 115 supra.

plaintiff had failed to allege facts as to her sufficient to state a cause of action for RPM in violation of the Cartwright Act. Had the plaintiff done so, though, the court observed that “if there were vertical price fixing, that would, under [Mailand v. Burckle], be a per se violation under the Cartwright Act, notwithstanding a change of law under the Sherman Antitrust Act, 15 U.S.C. section 1 et seq. [citing Leegin]. We are bound to follow the law set forth by our Supreme Court applying state law.”

To make itself even more abundantly clear, the court provided the following instructions to the trial court on remand: “For guidance of the trial court we note that the holding in [Mailand v. Burckle] that vertical price fixing is a per se violation of the Cartwright Act is the governing law of California.”

Some lessons to be learned from the state litigation thus far are these:

- State laws—or at least a state’s relative chances of success in challenging minimum RPM agreements—vary significantly by state.
- Relatively small companies may be more attractive targets in some states despite the potentially limited impact of their actions.
- Maximum RPM challenges are still “mostly dead.”
- Uniformity may be achievable only with the lowest common denominator.
- Franchisors should carefully consider especially their Internet sales and resale strategy.
- Franchisors should continue to weigh the incremental risks and benefits of minimum RPM agreements, especially given state law, franchisee relations, and business reality.

V. SO WHAT’S LEFT?

In light of the uncertain application of Leegin to RPM programs and the effective preclusion of national RPM programs as a result of state statutes or court decisions, what are franchisors desiring uniformity in pricing throughout their franchise systems to do? It is clear that, even after Leegin, a franchisor must at a minimum use caution in seeking to fix the price at which its franchisees resell products. But this does not mean that, even without application of Leegin’s principles, a franchisor’s hands are tied when it comes to franchisee pricing. To the contrary, franchisors may still influence franchisee pricing in a number of important ways that were developed in the pre-Leegin years, when minimum RPM remained per se illegal under federal law. These techniques, and their respective supporting principles, include the practices described below.

A. Setting a Price Ceiling, Not a Floor

Under the federal law since Khan, a franchisor can generally require its franchisees to participate in a marketing promotion that sets the price of a product at no higher than a predetermined price nationwide (e.g., a “99 cent-or-under” menu) or requires a particular discount off each sandwich (e.g., retail minus $1.00). In both cases, the promotion sets the price ceiling.

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123 Id. at *3.
124 Id. at *1.
and not the floor; franchisees are free to sell the sandwiches at an even lower price (or a steeper discount) if they choose.\textsuperscript{125}

The \textit{Khan} Court expressly recognized the \textit{Albrecht} Court’s “fear that maximum price fixing could be used to disguise arrangements to fix minimum prices,”\textsuperscript{126} but stated that “such conduct -- as with the other concerns articulated in \textit{Albrecht} – can be appropriately recognized and punished under the rule of reason.”\textsuperscript{127} Therefore, to avoid having a maximum price restriction construed as a disguised minimum RPM program (and thus subject to \textit{per se} treatment under at least some state laws), franchisees in any such program should remain free to sell products at a lower price than the specified maximum. In such circumstances, the arrangement should be analyzed under the rule of reason and generally not run afoul of Section 1 or state counterparts.

Notwithstanding the foregoing, there remains at least the theoretical prospect that a state may challenge a maximum RPM agreement under a \textit{per se} theory. For example, California’s statute quoted above does not distinguish between maximum and minimum price restrictions in its condemnation of price fixing. Further, an Assistant Attorney General for Antitrust in the California Attorney General’s office has observed that the California statute does not apply only to minimum RPM agreements, although she did acknowledge that limited resources would affect any determination to pursue a maximum RPM case.\textsuperscript{128}

\textbf{B. Unilateral Pricing Policy and Refusal to Deal With Violators}

Strictly speaking, prior to \textit{Leegin}, RPM was not considered \textit{per se} unlawful unless there was an actual agreement committing the franchisee or distributor to adhere to specific prices.\textsuperscript{129} As we shall see,\textsuperscript{130} however, any requirement to abide by a floor price, other than a truly unilateral, take-it-or-leave-it policy, would, as a practical matter, be viewed by courts as a tacit agreement between franchisors and franchisees to fix prices, and thus be considered \textit{per se} unlawful.

Because Section 1 of the Sherman Act only prohibits agreements or conspiracies in restraint of trade, a franchisor, like any supplier, may (at least in theory) simply announce its resale prices in advance and \textit{unilaterally} refuse to deal with those who refuse to comply.\textsuperscript{131} Such unilateral pricing policies are known as “Colgate” policies, after the Supreme Court decision that announced this principle. As the Supreme Court later explained in \textit{Monsanto Co. v. Spray-Rite Service Corp.}, “under \textit{Colgate}, a manufacturer can announce its resale prices in

\textsuperscript{125} Khan, 522 U.S. 3. But again, care must be taken to ensure that state law principles do not differ. See text accompanying notes 82 – 124 supra.

\textsuperscript{126} Id. at 16.

\textsuperscript{127} Id.


\textsuperscript{130} \textit{Infra} notes 139 – 166 and accompanying text.

advance and refuse to deal with those who fail to comply. And a distributor is free to acquiesce in the manufacturer’s demand in order to avoid termination.” 132 While manufacturers in numerous industries have successfully adopted such Colgate pricing policies, embarking on a unilateral pricing program is a complicated enterprise that, even in a post-Leegin world, should not be considered lightly.

First, the hallmark of any Colgate program is that it is truly “unilateral,” involving no concerted action with the resellers. Thus, the franchisor may not negotiate with non-compliant franchisees, but must terminate them (or at least their right to sell the products at issue) upon any violation of the policy. 133 For these reasons, while it is relatively easy to draft a Colgate unilateral-price policy, it is often quite difficult to enforce one, as it flies in the face of the common instinct to try to persuade recalcitrant franchisees to cooperate rather than terminate them on the spot.

Note that termination of a discounting franchisee following complaints by other franchisees does not necessarily imply an agreement on resale price, and challenges to such conduct have been frequently rejected. 134 However, under the Colgate line of cases, a franchisor may not terminate a price-cutting franchisee as part of an agreement (express or implied) with other, remaining franchisees to charge a set price. 135 In addition, if a franchisor imposes a price restriction as a direct result of pressure from other franchisees (and not because it is in the franchisor’s independent interest to do so) a court might find that such a “nominally vertical arrangement [was] in fact . . . a horizontal one in disguise,” and deem the conduct per se unlawful on those terms. 136

Second, many state franchise and distribution statutes prohibit unilateral termination of resellers except in certain narrow circumstances. 137 Thus, while a unilateral pricing program

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133 E.g., United States v. Parke, Davis & Co., 362 U.S. 29 (1960) (ruling that supplier may not seek promise from distributor to stop discounting); see JALA v. W. Auto Supply Co., 1995-2 Trade Cas. (CCH) ¶ 71,173 (D. Me. 1995) (“Acquiescence because of a fear of termination does not create an agreement.”) (quoting P. Areeda, Antitrust Law, ¶ 1451d, e at 127, 128 (1986)).

134 E.g., Euromodas, Inc. v. Zanella, Ltd., 368 F.3d 11, 26 (1st Cir. 2004) (no evidence of an agreement on price or price levels with the remaining distributor, as needed to establish per se violation); Ezso’s Invs., Inc. v. Royal Beauty Supply, Inc., 243 F.3d 980 (6th Cir. 2001) (application of the rule of reason proper where plaintiff failed to present evidence of a price agreement within the challenged vertical restraint); Rossi v. Standard Roofing, Inc., 156 F.3d 452 (3d Cir. 1998) (“were this simply a vertical conspiracy ... we would analyze it under the rule of reason unless there was some evidence of price fixing”); Bailey’s, Inc. v. Windsor Am., Inc., 1991-2 Trade Cas. (CCH) ¶ 69,627, at 66,814-15 (6th Cir. 1991) (summary judgment affirmed; termination after complaints of price discounting upheld in absence of agreement to set resale prices); The Jeanery, Inc. v. James Jeans, Inc., 849 F.2d 1148, 1160 (9th Cir. 1988) (JNOV upheld where no evidence that, in response to manufacturer’s coercive tactics, terminated dealer or other dealers communicated acquiescence to suggested price).


136 E.g., Ryko Mfg. Co. v. Eden Servs., 823 F.2d 1215, 1231 (8th Cir. 1987); Bus. Elecs., 485 U.S. at 720 n.4 (“[A] facially vertical restraint imposed by a manufacturer only because it has been coerced by a ‘horizontal cartel’ agreement among its distributors is in reality a horizontal restraint.”).

137 See, e.g., Wisconsin Fair Dealership Law, Wis. Stat. § 135 (prohibiting termination or substantial change in competitive circumstances of franchisee, distributor or dealers without cause and opportunity to cure). Consider also whether the broad wording of some state antitrust statutes could cover nominally unilateral RPM arrangements. See notes 82 – 101 supra. Finally, the entire concept of Colgate or unilateral pricing programs is facing heightened scrutiny in certain industries. See, e.g., Utah Code § 58-16a-905.1 (“A contact lens manufacturer or a contact lens
calling for termination of recalcitrant distributors/franchisees might be permissible under the Sherman Act even before *Leegin*, it might nevertheless violate state franchise or distribution law. Careful review of all applicable state laws is therefore critical before embarking on any *Colgate* pricing program.

C. "Suggested" Resale Prices

Even before *Leegin*, it was clear that franchisors may properly provide their franchisees with *suggested* resale prices, whether in the form of price lists, menu boards, pre-ticketed items or otherwise. Such suggestions are not unlawful, even if the franchisees ultimately adhere to the recommended pricing, so long as each franchisee “independently decides to observe specified resale prices.”

A much-litigated issue has been whether a seller, by unduly aggressive tactics, can be said to have coerced a buyer’s adherence to a certain price, thereby engaging in collective action. Such tactics as penalizing non-cooperating dealers in product allocation and delivery, requiring approval of deviations from suggested pricing, and threats and imposition of sanctions for noncompliance have been deemed evidence of coercion.

At the same time, some courts have upheld actions that come quite close to actual coercion. In *Curry v. Steve’s Franchise Co.*, for example, an ice cream shop franchisor provided its franchisees with a menu board that stated the prices for the various ice cream products sold at the store. After the franchisee raised prices by 10% (this case was pre-*Khan*), a representative of the franchisor visited the franchisee’s stores and physically altered the prices on the stores’ menu boards and cash registers. On the franchisor’s motion to dismiss franchisee’s resale price maintenance claims, the district court concluded that,

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138 The well-established law in this area may serve as a limitation on franchisors’ ability to adopt *Leegin* programs, as many franchisors embedded that law in their systemwide franchise agreements, through the use of clauses such as “Franchisor may from time to time recommend or suggest resale prices for use by Franchisee, but Franchisee shall at all times remain free to establish in its own discretion the resale price for products to be sold by Franchisee.”


140 *E.g., Acquaire v. Canada Dry Bottling Co. of N.Y., Inc.*, 24 F.3d 401, 410 (2d Cir. 1994); *Gray v. Shell Oil Co.*, 469 F.2d 742, 748 (9th Cir. 1972).


142 *See Yentsch v. Texaco, Inc.*, 630 F.2d 46, 53 (2d Cir. 1980).


144 Id. at *4.
notwithstanding the representative’s actions, the franchisees were not coerced or harassed into maintaining resale prices, in part because the franchisee did not allege that the franchisor threatened “adverse consequences of noncompliance.” “Exposition, argument or persuasion are distinct from coercion. . . . The [franchisee's] affidavit does not indicate that [his] independent discretion as to pricing was not maintained.” 145 Of course, a different court might have viewed the facts differently and concluded that the franchisor’s conduct crossed the line.

In a more recent decision, *Steak N Shake Enters. v. Globex Co., LLC*,146 the termination of two Colorado Steak 'n Shake franchisees, based upon their refusal to offer customers the “4 Meals Under $4” promotion required by the franchisor, was upheld. The District Court’s decision does not address antitrust issues at all, and the terminated franchisees’ claims under the Colorado Consumer Protection Act had been withdrawn prior to the court’s decision. Instead, the court analyzed the case as a straightforward breach of contract case – the subject franchise agreements had, among other things, required the franchisees to adopt the franchisor’s standard menu and to participate in all local, regional, seasonal, promotional and other programs – and found that the franchisees had knowingly and materially breached their franchise agreements.

D. **Consignment and Agency Arrangements**

Where there is no “sale” of product to a franchisee for resale, franchisors and suppliers cannot be liable for price fixing. Thus, if a franchisor supplies products to end users via its franchisees under a genuine consignment arrangement, without transferring control, title and risk of loss in that product to the franchisees, then the franchisor generally can set the resale price unilaterally.147 Similarly, franchisors do not engage in unlawful RPM when they set the price at which their commissioned sales agent or employee must sell products.148 The question in many cases is whether a true agency relationship exists between the manufacturer and its resellers.149 As with *Colgate* programs, trying to fit a franchisee pricing program under this “agency” rubric can raise numerous other complications and should not be considered lightly.150

145 *Id.* at *3.


148 See, e.g., *Day v. Taylor*, 400 F.3d 1272, (11th Cir. 2005) (examining indicia of agency to conclude that U-Haul’s relationship with its independent dealers was genuine agency).

149 *E.g., Simpson*, 377 U.S. at 13 (finding that the alleged consignment/agency relationship between supplier and distributor was a sham used to establish resale price maintenance). See also *U.S. v. Apple, Inc.*, 952 F.Supp.2d 638 (S.D.N.Y. 2013), aff’d __ F. 3d __ (2nd Cir. 2015) (e-book publishers unsuccessfully adopted the agency structure to maintain e-book prices at a level above Amazon.com prices. Finding that the arrangements constituted a “hub-and-spoke” conspiracy among the publishers, rather than a series of agency agreements between Apple and individual publishers, led the Court of Appeals to find the arrangements illegal on a *per se* basis.)

150 For example, a true agency relationship with franchisees can give rise to liability and other issues that franchisors often strive to avoid.
E. Advertising Prices

Franchisors may generally advertise their “suggested” prices directly to the consumer – for example, a nationally-advertised “99¢ Menu.” Although franchisees might feel pressure to comply with the pricing once consumers are aware of it, courts have held that such direct-to-consumer advertising does not constitute “coercion” sufficient for a finding of antitrust conspiracy.\(^{151}\) Thus, a franchisor might make a suggested pricing program “voluntary” for franchisees, while advertising the prices directly to consumers to obtain compliance without an “agreement.”\(^ {152}\) In fact, in *Jack Walters & Sons Corp. v. Morton Building, Inc.*, Judge Posner, writing for the court, found no conspiracy to fix prices where the manufacturer exerted some pressure on dealers to comply with nationally advertised prices, concluding that:

> [I]f it is lawful to advertise a retail price, it should be lawful to take at least the minimum steps necessary to make that advertising beneficial. It would be pretty embarrassing for a manufacturer who had advertised a special retail price to be bombarded by complaints from consumers that dealers were refusing to sell to them at that price. Such refusals would make the advertising misleading and might even expose the manufacturer to legal sanctions under the Federal Trade Commission Act or counterpart state regulations. . . . [Thus, the defendant] had to pressure its dealers to lower price in order to maintain the credibility of its price advertising.\(^ {153}\)

Cooperative advertising programs that contain price restrictions – i.e., where advertising co-op funds are available only for advertisements that comply with the manufacturer’s suggested pricing – were once considered close enough to actual coercive price maintenance to warrant treatment as *per se* unlawful.\(^ {154}\) However, the Federal Trade Commission subsequently determined that cooperative advertising arrangements should be analyzed under the rule of reason, so long as the arrangements do not limit the dealer’s right: (1) to discount below the advertised price, and (2) to advertise at any price when the dealer itself pays for the advertisement.\(^ {155}\) Cooperative advertising programs that deny co-op payments to retailer advertisements that include prices below a “minimum advertised price” (“MAP”) have generally been upheld under the rule of reason, so long as the retailers are allowed to advertise below the MAP at their own expense, and to sell below MAP.\(^ {156}\)

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\(^{151}\) *E.g.*, *Acquaire v. Canada Dry Bottling Co.*, 24 F.3d 401 (2d Cir. 1994); *Jack Walters & Sons Corp. v. Morton Bldg., Inc.*, 737 F.2d 698 (7th Cir. 1984).

\(^{152}\) Note, however, that to avoid liability for false advertising, direct-to-consumer advertising of this sort generally must carry an “at participating stores only” caveat. *E.g.*, *Murphy v. White Hen Pantry, Bus. Fran. Guide (CCH) ¶ 7716*, No. 79-C-460, 1981 WL 2215, *3-4* (E.D. Wis. Aug. 6, 1981), aff’d, 691 F.2d 350 (7th Cir. 1982).

\(^{153}\) *Jack Walters*, 737 F.2d at 708. Note, however, that because *Jack Walters* involved manufacturer pressure to lower prices, rather than raise them, the rule of reason would likely apply under *Khan* even without the subsequent holding in *Leegin*.


Note, however, that a prohibition on advertising below MAP regardless of whether or not the manufacturer is contributing to the costs of the advertising, and particularly where the restrictions effectively prevent sales at discount prices, have proven far more problematic. The FTC in a series of cases in the year 2000 entered into consent orders restricting the major music companies from making their retailers' receipt of cooperative advertising or other promotional funds contingent on MAP that included prohibitions on all discount advertising, including ads funded by the retailer and those in the store itself. In these cases, collectively referred to as the “CD-MAP cases,” the music companies' restrictive rules were deemed to effectively prevent any discounting, and were therefore found to be per se illegal.

The CD-MAP cases illustrate that, at least under pre-Leegin law, a franchisor could not prohibit its franchisees from advertising prices below the franchisor’s suggested resale prices if the effect of the prohibition would be to prevent franchisees from selling at prices lower than the suggested resale price. The prevalence of internet retailing illustrates how fine this line may be to walk in practice. In brick-and-mortar franchises – where there is actually a “store” for consumers to visit – a MAP restriction that is properly limited to off-premises advertising would generally not limit the franchisee’s ability to sell at lower prices. If a franchisee exists solely on the internet, however, any franchisor-imposed restriction on advertising prices below MAP might also be deemed to restrict the franchisee’s ability to sell its product at lower prices through its website.

F. Internet Advertising Restrictions

Advertising restrictions may become more problematic on the internet, where the point of advertising is also the point of sale. So-called internet minimum advertised price (“IMAP”) programs generally preclude the advertisement of discounted prices on internet websites. Put simply, the question becomes how to distinguish between a mandated advertised price and a mandated sales price on the internet. Many suppliers require the advertisement only of the suggested retail price along with each product’s description but permit the actual sales price to be displayed once a purchaser has moved an item into his or her online “shopping cart.”

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158 E.g., D. Balto, Emerging Antitrust Issues In Electronic Commerce, 1999 ANTITRUST INSTITUTE DISTRIBUTION PRACTICES: ANTITRUST COUNSELING IN THE NEW MILLENNIUM (November 12, 1999), 1999 WL 1065039, at *15 ("If the website is not simply an advertisement, but takes purchase orders as well – the business is true electronic commerce, in other words – the prices listed are both part of the advertising and the equivalent of in-store price stickers, suggesting that the MAP restrictions would be the exact functional equivalent of resale price maintenance.").

159 Compare Worldhomecenter.com, Inc. v. L.D. Kichler Co., 2007 WL 963206 (E.D.N.Y. March 28, 2007) (stating that a contested IMAP policy had the effect of restricting retail prices for internet retailers), with Campbell v. Austin Air Sys., Ltd., 423 F. Supp. 2d 61 (W.D.N.Y. 2005) (holding that the IMAP policy at issue restricted only the advertised price and had no price-fixing implications).

160 See Rosch, supra note 113, at 22.
Although this practice is fairly common among online retailers, the courts have not yet provided definitive guidance on the practice.

G. Promotional Pricing and Requiring Pass-on to Downstream Retailers or Consumers

Following from the general rule that setting maximum prices, rather than minimum, has generally been viewed as procompetitive and beneficial to consumers, manufacturers may require that their distributors pass on discounts to downstream retailers or consumers, where the arrangement does not prohibit the distributor from offering greater discounts than the manufacturer provides. They may also adjust their pricing to distributors based on competitive changes in the resale market, again so long as they do not actually mandate resale prices.

Franchisors may also have more leeway in requiring franchisees to adhere to special pricing in a limited-time promotional setting, especially where the franchisor bears the burden of the discount, either by reducing its wholesale prices or by providing money back to the franchisees as a credit, rebate, or contribution of advertising dollars. For example, in Jack Walters, the Seventh Circuit upheld a manufacturer’s efforts to ensure that its dealers complied with special promotional pricing where the manufacturer gave the dealers a discount from the wholesale price to make it easier for them to offer consumers the special retail price, and the manufacturer wanted that discount to inure to the benefit of the consumers, not the dealers. Thus, the manufacturer’s actions in advertising the special price directly to consumers and monitoring its dealers to ensure that they sold product at no more than the advertised price were lawful.

VI. CONCLUSION

As demonstrated by this paper, Leegin has established new rules for the assessment of minimum RPM programs under federal law but, because of the factors discussed above, its impact on national franchising has not been as significant as originally anticipated. Although the hope had been that Leegin would bring clarity to a somewhat murky subject, it demonstrably has not. The question we are left with is whether Leegin’s progeny, potential state law developments or even federal legislation may reasonably be expected to further shape the existing ill-defined contours of RPM law.

161 Id.

162 Compare Worldhomecenter.com, Inc. v. L.D. Kichler Co., 2007 WL 963206 (E.D.N.Y. March 28, 2007) (stating that a contested IMAP policy had the effect of restricting retail prices for internet retailers), with Campbell v. Austin Air Sys., Ltd., 423 F. Supp. 2d 61 (W.D.N.Y. 2005) (holding that the IMAP policy at issue restricted only the advertised price and had no price-fixing implications).

163 See AAA Liquors, Inc. v. Joseph E. Seagram & Sons, 705 F.2d 1203 (10th Cir. 1982) (a manufacturer who grants a discount from its own pocket through a distributor to its retailer has a legitimate interest in making sure that the distributor is not pocketing the price support instead of passing it on; it is not thereby coercing compliance with resale price).

164 E.g., Sun Oil Co. v. FTC, 294 F.2d 465 (5th Cir. 1961), rev’d on other grounds, 371 U.S. 505 (1963).

165 Jack Walters, 737 F.2d at 709.

166 Id.
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Allan P. Hillman is a partner with Kern & Hillman LLC in Hamden, CT. A graduate of Columbia College and Columbia University Law School, he has practiced, taught and written on franchise, antitrust and intellectual property law for over forty years, and currently is a member of the Governing Committee of the ABA Forum on Franchising. He is a past chair of the Connecticut and Maryland Bar Associations’ Franchise, Distribution and Dealer Law sections and of the Maryland Bar Business Law section.

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Allan has been a frequent speaker at ABA Forums on Franchising and at the IFA Legal Symposia. He was awarded the inaugural “Hillman Award,” for the “Funniest Lawyer in Maryland,” and won it a second time before leaving the state (but not his Maryland practice) to reunite with his true love in 2006.

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