Resale Price Maintenance: Real Life Lessons from a Mock Trial

Michael A. Lindsay

Practitioners have had little guidance on how a jury would actually evaluate a challenge to resale price maintenance (RPM) under the rule of reason—and what a jury's evaluation might teach the counselor about structuring an RPM program in the first place. That is because, for almost a century, RPM agreements have been treated as illegal per se under both state[1] and federal antitrust laws[2]—illegal, that is, because courts presumed, rather than required proof of, actual anticompetitive effects in the particular factual setting of the agreement.

For decades, however, economists have urged various justifications for RPM programs, suggesting that in many cases an RPM program can be procompetitive. These arguments have been in the ascendancy for many years and played a major role in the Supreme Court's 2007 decision in *Leegin*,[3] overruling the per se rule established in its 1911 *Dr. Miles* decision.[4]

The rule of per se illegality for RPM agreements meant that real-life litigation always turned on whether there was an *agreement* between the manufacturer and one or more of its resellers, as opposed to the manufacturer's unilateral adoption and announcement of a *policy*. If the finder of fact determined there was an "agreement" to charge a specific price or price level, the agreement was judged illegal per se, eliminating the need to ascertain whether it had actual, unreasonable economic effects in the particular circumstances. In contrast, a manufacturer's unilateral policy was not an "agreement" to which Section 1 of the Sherman Act could apply, even if the resellers chose to follow the policy—presumably yielding the very same economic effects as a banned agreement and, once again, no occasion to investigate whether it produced actual, unreasonable economic effects.

Elimination of the per se rule (at least in cases brought under Section 1 of the Sherman Act[5]) means that issues that have lain dormant for almost a century must now be addressed. These include (1) what must be proven to establish that an agreement between a manufacturer and its individual resellers on resale prices violates the rule of reason, (2) how will juries respond to evidence offered to show or rebut a rule of reason violation, and (3) how do the outcomes shape advice to sellers considering such resale price agreements?

■

Michael A. Lindsay *is a partner with Dorsey & Whitney LLP in Minneapolis and is co-chair of the firm's Antitrust Practice Group. He is a vice-chair of the Antitrust Section's Trial Practice Committee and served as session chair and moderator for the mock trial. He thanks Tasneem Chipty, Leslie Ellis, David Faith, Bob Hubbard, Andrew Rossner, and Lawrence Wu for their comments on an earlier draft of this article.*

[1] Only one state statute expressly provides that RPM agreements are judged under the rule of reason. *See* Gilbert's Ethan Allen Gallery v. Ethan Allen, Inc., 620 N.E.2d 1349, 1356 (Ill. App. Ct. 1993) (vertical price-fixing agreements are to be tested under rule of reason because "per se violations are normally agreements between competitors or agreements that would restrict competition and decrease output"; federal case law is instructive but not binding), *aff'd*, 162 Ill. 2d 99 (1994). For discussion of state laws, see Michael A. Lindsay, *Resale Price Maintenance and the World After* Leegin, ANTITRUST, Fall 2007, at 32; Michael A. Lindsay, *Overview of State RPM (Complete)*, ANTITRUST SOURCE, July 2007, http://www.abanet.org/antitrust/at-source/07/12/LindsayFullChart11-29.pdf.

[2] Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911).

[3] Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 127 S. Ct. 2705, 2713 (2007).

[4] 220 U.S. 373 (1911).

[5] 15 U.S.C. § 1.

The ABA Antitrust Section's 2008 Spring Meeting Mock Trial program took a first step in addressing these issues. Every year the Trial Practice Committee (TPC) presents a mock trial at the Section's Spring Meeting. The program presents experienced counsel trying a case—in a highly compressed format—before a live jury and a federal judge.[6] The jury, selected from the Washington D.C. area, hears opening statements, direct and cross-examinations, closing arguments, and jury instructions, all in about two-and-a-half hours. The jury then retires to deliberate for forty-five minutes to an hour, and the audience is able to watch the deliberations through closed-circuit television. The jury returns after its deliberations, renders a verdict, after which each juror tells a little about himself or herself, and audience members are invited to ask questions. This year's mock trial presented a post-*Leegin* challenge to resale price maintenance under the rule of reason.

Facts of the Case

The agreement permitted FMG to set manufacturer's suggested retail prices (MSRPs) and required retailers to sell at or above that price.

Video-game manufacturer Futuristic Multi-Player Gaming, Inc. (FMG) makes multi-player "shoot-em-up" and sports video games. FMG began requiring its resellers to sign agreements with express minimum RPM provisions. An unnamed state, represented by lawyers from the Attorneys General offices of New York and New Jersey, brought suit against FMG in federal district court under Section 1 of the Sherman Act, challenging these agreements under the rule of reason. The price agreement was explicit and undisputed, so the defense could not assert a *Colgate* defense based on lack of agreement.

In 2000, FMG was the market leader in multi-player gaming products,[7] with a revenue share of about 60 percent. The market was fairly concentrated, with the top three firms accounting for about 90 percent of sales. In 2001, the demand for gaming products collapsed, the result of a weak 2001 holiday shopping season and consumers' general distaste for ultra-violent shoot-em-up games in the wake of the 9/11 attacks. Retailers were left with excessive inventories of unsold FMG games, which led to extreme retail price cutting.

FMG, after investing substantial resources, succeeded in developing significantly improved features. Nevertheless, most retailers declined to carry FMG products because of personal or institutional memories of the disastrous losses in 2001. As a result, FMG's performance in 2002 and 2003 was miserable, and the company teetered on the edge of bankruptcy. Then in early 2004, new management was brought in. Management recognized FMG's significant technological advantages, but the company still had severe difficulties persuading retailers to carry its products.

FMG's response was the Retailer Protection Program (RPP), introduced before the 2004 buying season. Under the RPP, every retailer that sold FMG products signed an RPM agreement. The agreement said all the "right" things that a well-counseled manufacturer would likely include (or at least most of them). It described the procompetitive purposes for the agreement, specifically, to encourage customer service, premium image, product promotion, prevention of free-riding, and fair returns to retailers.[8] The agreement permitted FMG to set manufacturer's suggested retail

---

[6] The Hon. Loretta Preska of the Southern District of New York presided. The states were represented by Bob Hubbard and Andrew Rossner, and the defendant FMG by M. Sean Royall and Margaret Zwisler. The state's witnesses were portrayed by James Yoon and Tasneem Chipty, and FMG's by Carol Peterson and Lawrence Wu. Leslie Ellis and TrialGraphix arranged the jury and provided trial support to both sides.

[7] The facts were simplified by ignoring any proprietary platforms—the gaming software was compatible with any platform.

[8] The agreement stated: "The purposes of the RPP are to promote customer service, preserve and enhance FMG's brand image as a premium manufacturer of video games, reduce free riding by retailers, ensure that retailers receive sufficient return on their investments to provide the level of customer service necessary to support and promote FMG products, and ensure sufficient retail outlets for FMG products."

prices (MSRPs) and required retailers to sell at or above that price. The agreement prohibited all discount devices (coupons, rebates, and the like). FMG could identify products as close-outs, permitting retailers to sell below MSRP. Retailers were required to participate in in-store promotions, displays, and/or demonstrations of FMG products; they were also required to maintain ample FMG inventories. FMG could terminate retailers for noncompliance. In fact, FMG sent hundreds of warning letters and terminated twenty-five to one hundred retailers in each of the three years the program was in effect. FMG was the only firm in the industry that adopted an RPM program.

Additionally, it was uncontested that prices increased since the product crash of 2001, but product quality had improved as well. Some competitors complained about the inability to obtain shelf space for their competing products, but other firms appeared to be expanding.

The Trial

The jury processed in shortly after 1:30 p.m. and retired a bit before 4:00—about two-and-a-half hours for trial of a complex economic issue. The trial began with opening statements.[9] The State presented two witnesses: a video-game retailer whom FMG had terminated for below-MSRP sales, and an economist who explained how the program had resulted in higher prices for consumers. The defense also presented two witnesses: the FMG Vice President of Marketing, who had developed the program, explained the dire circumstances that had motivated the company's decision, and an economist explained the value of the program in promoting interbrand competition.

In closing arguments the State contended that the program was designed to protect retailers from competition and resulted in higher prices for consumers. The defense argued that the program helped consumers by inducing retailers to carry FMG products and to provide retail services. In rebuttal, the State argued that an RPM policy was not justified to address demand uncertainty and inventory risk even in the immediate aftermath of the 2001 pricing debacle,[10] although its economist recognized that possibility.

Instructions

The divergent views of the mock trial counsel and their natural (and commendable) desire to win combined for a potent cocktail when it came time for the jury instructions. After multiple conference calls and skillful arguments on both sides, the Trial Practice Committee arrived at a fairly balanced set of instructions and verdict form intended to implement the principles of *Leegin*.[11] The

---

[9] To conserve program time for trial and deliberations, the jury had been instructed on certain procedural matters before the mock trial program began.

[10] When the demand for a product is uncertain, a retailer cannot reasonably predict how much of the product will be sold at the contemplated resale price—and thus how much product to order. The retailer will fear being saddled with unwanted inventory, which he may have to sell at heavily discounted prices, perhaps even at a loss. This fear will cause the retailer to order and carry less inventory. By guaranteeing stable prices in periods of low demand realization, an RPM program can help mitigate some of the inventory risk. When demand turns out to be low and the manufacturer's minimum resale price is higher than the true market-clearing price, retailers will not resort to a discounting war to attract the available consumers because discounting will be prohibited. Sales may be slower, and the retailer may still end up with unsold inventory, but the profits at the RPM price may be sufficient to cover the excess-inventory losses. *See generally* Raymond Deneckere, Howard P. Marvel & James Peck, *Demand Uncertainty, Inventories, and Resale Price Maintenance*, 111 Q.J. Econ. 885 (1996).

[11] Although agreeing to the instructions for the Mock Trial program, the State's mock-trial counsel did not concede the propriety of using nonprice vertical restraint principles for an RPM agreement. For an illustration of state views on how *Leegin* should be construed, see Amended States' Comments Urging Denial of Nine West's Petition, Nine West Group Inc., FTC Docket No. C-3937 (Jan. 17, 2008), *available at* http://www.oag.state.ny.us/business/new_antitrust/antitrust_amici_new.html. *See also* Robert L. Hubbard, *Protecting Consumers Post-*Leegin, Antitrust, Fall 2007, at 41.

instructions and verdict form have been posted on the Trial Practice Committee's Web site.[12]

Where possible, the instructions were drawn substantially from the Antitrust Section's *Model Jury Instructions in Civil Antitrust Cases*[13]—for example, for basic information on the Sherman Act, unreasonable restraints of trade, the rule of reason, and the balance of harms. The Section's model instructions pre-dated *Leegin*, however. This required modifying some instructions. Some of this material came directly, or in slightly paraphrased form, from *Leegin*. For example, one instruction offered examples of when an RPM agreement might be lawful and when it might not.[14]

The jury was asked to consider, first, whether the State had proven that FMG's contract resulted in substantial harm to competition. If so, the jury was asked to determine whether the restraint also benefited competition in other ways. If the jury found competitive benefits, then the jury was next instructed to consider whether the restraint was reasonably necessary to achieve the benefits. Finally, the jury was asked to weigh any competitive benefits against any competitive harm resulting from the contract. The court reminded the jurors that they must consider the benefits and harm to competition and consumers, not just to a single competitor or group of competitors.

Indeed, of the nine jurors, only two were able to see any procompetitive benefit . . .

To help the jury in its task, the instructions included explanations of interbrand versus intrabrand competition, price versus non-price competition, and the role of market power. At each stage the instructions made clear that the State had the burden of proof; there was no formal burden for the defense to justify the RPM agreements.

Deliberations

What, then, happened when these facts were handed to the jury? Not every jury will have, like this mock jury, a graduate student who talks of "doing a cost-benefit analysis" in an antitrust case. Nevertheless, lawyers who have drunk deeply from the *Leegin* majority opinion had a rude awakening. The scholarly arguments about interbrand versus intrabrand competition, and the need to enable investment by preventing free-riding, did not have much traction with this particular mock jury. Indeed, of the nine jurors, only two were able to see any procompetitive benefit to FMG's resale price maintenance agreements. Even those two believed these benefits were outweighed by the anticompetitive harm.

The jury reached its decision easily and quickly. They were able to rule in favor of the State after answering the first two questions on the special verdict: "Did the FMG agreement with resellers substantially harm competition in the relevant market?" and "If the FMG agreement substantially harmed competition in the relevant market, did it produce any procompetitive benefits in a relevant market?"[15] With the jury's answers of "yes, substantial harm" and "no benefits," it was, to use an expression apropos of the fact pattern, "game over."

---

[12] Jury Charge, *available at* http://www.abanet.org/antitrust/at-committees/at-trial/pdf/jury-instructions/preska.pdf; Special Verdict Form, *available at* http://www.abanet.org/antitrust/at-committees/at-trial/pdf/jury-instructions/resale-verdictform.pdf. The instructions as actually delivered were modified slightly but not substantively.

[13] ABA Section of Antitrust, Model Jury Instructions in Civil Antitrust Cases (2005 ed.).

[14] Instruction No. 9 in Jury Charge at 12, *available at* http://www.abanet.org/antitrust/at-committees/at-trial/pdf/jury-instructions/preska.pdf ("Agreements establishing minimum resale prices can have either procompetitive or anticompetitive effects or both. A manufacturer may use resale price maintenance for the procompetitive purpose of encouraging retailers to invest in services or promotional efforts that aid the manufacturer's position as against rival manufacturers. On the other hand, a powerful manufacturer can use resale price maintenance for the anticompetitive purpose of giving retailers an incentive not to sell the products of smaller rivals. If FMG's contract has not substantially harmed competition in the relevant market, then you should find that FMG's contract was not unreasonable.").

[15] Special Verdict Form, *available at* http://www.abanet.org/antitrust/at-committees/at-trial/pdf/jury-instructions/resale-verdictform.pdf.

Some Real-Life Lessons for Trial Lawyers

The outcome of the mock trial should not be overstated, because the compressed nature of the exercise certainly affected the defense team's ability to develop its arguments. Nevertheless, the trial did yield some specific lessons and useful reminders of probable juror concerns that counselors and trial lawyers should consider:

1. Know the Audience. One of the jurors put the point very clearly: "We're all consumers." The plaintiff can play to this expressly, as the State's counsel in the mock trial artfully demonstrated. But for a defendant to come in and say "I'm a manufacturer and I want to charge you higher prices" is not an easy sale to make to this audience, even when you add "but it's good for you—really." Defense counsel in the mock trial were keenly aware of this issue and addressed it head on. All counselors and trial counsel should think carefully about how they can present to a jury of consumers a case whose consumer appeal may not be immediately apparent.

One of the jurors put the point very clearly: "We're all consumers."

2. Emphasize Consumer Benefits. The mock jury's instinct—that antitrust laws exist to help consumers—is essentially correct. If a defendant plans to argue, "but it's good for you," the defendant should be able to articulate how—i.e., better services, broader selection, longer store hours, whatever the additional increment the plan is intended to encourage. This depends in the first instance on the reasons behind the program's conception and implementation. In this trial, the State's counsel were able to make effective use of the very title of the program—the *Retailer* Protection Program—as evidence that the program did not help consumers—and thereby to undermine claims of consumer benefits.

3. Embrace the Practical Burden. The jury instructions made clear that the State bore the legal burden of proving that the agreements illegally restrained trade, but the lopsided view from the jury room made clear that no matter what the instructions said, the defendant will likely have a *practical* burden to justify the program. A defendant should openly acknowledge, for example, that some consumers (the more sophisticated) may not need the pre-sale services and that all consumers will pay more than they might otherwise pay. An advocate may be better off conceding what jurors are already likely to believe, which may increase the advocate's credibility when arguing the restraint provides consumer benefits.

4. Explain the Competitive Process. Jurors bring their own experience to bear, but for the most part they have only been at the consumer end of the purchasing process. Trial counsel should find a good teacher to help the jury to understand the competitive process and the role that RPM plays in it. Given the jurors' likely consumer-oriented viewpoint, defense counsel should make sure that this teacher has adequate time for the task. (One of the byproducts of our mock trial's compressed format was that the defense's excellent testifying economist did not have enough time.)

5. Defend the Value of Choice. One variation on consumer benefits is choice—the ability of consumers to decide whether they want the pre-sale services. The plaintiff's counsel will emphasize that consumers should not have to pay for services they do not want. Defense counsel should counter with two points—first, that many consumers do want these services, and second, that consumers who do not want to pay for these services can buy someone else's product or go to someone else's store—there's usually plenty of choice.

6. Defuse the Injured-Competitor Argument. Jurors will sympathize with an excluded competitor, even if there are good economic reasons for the exclusion. In this case, the challenged agreements did not explicitly deny shelf-space to FMG's rivals, but the State was able to argue that they had an exclusionary effect.

7. Explain Adequacies (or Inadequacies) of Alternatives. Very often, suppliers can use non-price arrangements to provide dealers with incentives to provide point of sale service and other sales

effort. The mock jury closely scrutinized FMG's arguments for choosing RPM rather than these alternatives, to the extent that it was willing to give those arguments any credence at all. In a sense, the jury applied a rough "least restrictive alternative" test. A trial lawyer defending an RPM program must prepare to explain why non-price alternatives were unavailable, inadequate, or less desirable.

8. Address Retailer Independence. Shortly after *Leegin* was decided an anonymous comment posted to the *Wall Street Journal*'s law blog observed that "the 'small dealers and worthy men' argument consistently loses in antitrust, as well it should. [I]f every mom and pop store goes out of business, well, so be it—they can't compete with [Wal-Mart]."[16] Suffice it to say that this was not the mock jury's view. Although most of the jurors looked at the case from their perspective as consumers, at least one of the jurors also looked at it from that juror's perspective as a retired independent business owner—and expressed concern about the retailer's loss of independence in making business decisions. Trial counsel should remember that the fate of small, independent retailers can still concern jurors.

9. Defend Fairness. An RPM case is like any other—the jury wants to know that the result is fundamentally fair. In the mock trial, defense counsel did an excellent job of explaining the unfairness of free-riding and the fairness of preventing it. But one of the mock jurors spotted something in the facts: FMG's program required retailers to charge MSRP but did nothing to protect the retailer if the product did not move at those prices. In other words, without some kind of inventory buy-back provision, an RPM program may be perceived as leaving the retailer with all of the inventory risk while depriving the retailer of the ability to manage inventory through price adjustments.

Real-Life Lessons for Antitrust Counselors

The *Leegin* decision does not make RPM agreements per se lawful, and the mock jury's deliberations suggest that, in a jury trial, RPM agreements may well be found anticompetitive. Even setting aside the uncertainty caused by some real-life states' unwillingness to abandon the pre-*Leegin* framework,[17] successful defense of an RPM agreement in front of a jury is far from assured. Counselors helping companies to develop RPM programs (and advising on whether to adopt such programs at all) should consider how a program is likely to play before a jury, because that will provide practical guidance as to the wisdom and workability of an RPM program. Moreover, it may suggest ways of describing the program and educating company employees and resellers about how and why the program works—and how it helps consumers.

In addition to taking to heart what trial lawyers will ultimately face, counselors should also consider these points:

1.* Colgate *Is Still a Fine Decision. Given the difficulties that a defendant will face at trial if its RPM program is challenged under the rule of reason, counselors should not be too hasty in abandoning the *Colgate* principle. A *Colgate* approach, using a unilateral policy instead of entering into an agreement, provides a first defense against RPM claims and also pays at least nominal tribute to the retailer's independence. If a client nevertheless decides to implement a program based on agreements with retailers, the counselor should consider first the risk mitigators that might prevent the program's ever reaching a jury, or help a jury to understand and accept it.

---

[16] Peter Lattman, *The Supreme Court Disses* Dr. Miles (Jun. 28, 2007), http://blogs.wsj.com/law/2007/06/28/the-supreme-court-disses-dr-miles/ (third comment). The commentator was alluding to a phrase from *United States v. Trans-Missouri Freight Association,* 166 U.S. 290, 323 (1897).

[17] For example, just days before the mock trial, three states entered into an RPM consent decree. *See* New York v. Herman Miller, Inc., 08 Civ. 2977 (S.D.N.Y. Mar. 25, 2008) (Stipulated Final Judgment and Consent Decree).

2. Market Share Matters. A company's small market share is one factor that can reduce risk of pursuing an RPM program. Companies with low market shares are less likely to have their programs reach the jury, and if one does, they have an avenue to deflect claims of consumer harm, as the Federal Trade Commission's recent decision modifying the *Nine West* consent order suggests.[18] Counselors should be particularly cautious if the company proposing an RPM program has a substantial market share, especially in a concentrated market.

3. Pick the Right Product. Some products warrant pre-sale services, and in those cases consumers can benefit. The mock trial facts and exhibits included material to help strengthen the arguments of consumer benefits—for example, trade press reports of stores hiring unemployed gamers to demonstrate FMG products, share tips and strategies, and play with potential buyers, all resulting in managers claiming that this strategy had increased store traffic. That will not be true for all products. At the end of the day, the jury will ask the same question that senior managers and their counselors should have asked at the outset: do pre-sale services really add value for consumers and result in increased sales and consumer satisfaction?

4. Consider the Alternatives. Many clients have heard about the *Leegin* decision and may assume that an RPM program is the right tool for them. Counselors should question the client closely on the underlying problem and determine whether an RPM program is a good fit. For example, if the real problem is too many resellers in too close proximity to one another, an RPM program is not likely to be the answer—but cleaning up the distribution network may be.

5. Address the Inventory Problem. Product shortages may not undermine an RPM program, but excess inventory carries that risk. Companies and their counselors should consider the implications of an RPM program on inventory management. Should resellers be limited in how much product they can order? What happens if the reseller orders more product than the RPM program price will permit it to sell? Will the manufacturer have a liberal return policy? Will it buy back inventory from terminated resellers?

6. Get the Program Rationale Right the First Time—and Keep It That Way. A company may some day have to explain its RPM program to a jury. This means that, from the beginning, the company and its counselors need to understand why the company is adopting the program and make sure that it is a defensible rationale. All communications that refer to the program—including internal discussions, as well as external materials such as program materials for resellers, public Web sites, account manager communications—should all reflect and be consistent with the program's procompetitive rationale.

Conclusion

RPM programs still run risks for suppliers, as the results of the mock jury trial demonstrated. A successful RPM program therefore will be one whose rationale a jury can understand. That means its rationale should include a convincing and accessible demonstration of how the program, as designed, described, and operated, helps consumers. ●

---

[18] Order Granting In Part Petition To Reopen And Modify Order at 15, Nine West Group Inc., FTC Docket No. C-3937 (Apr. 11, 2008), *available at* http://www.ftc.gov/os/caselist/9810386/080506order.pdf ("Nine West has only a modest market share in any putative relevant product market in which it competes. This suggests prima facie that it lacks market power, and there is no reason to believe that there is collective market power in any putative market. There is also no evidence of a dominant, inefficient retailer in this market, and Nine West states that Nine West itself is responsible for its desire to engage in resale price maintenance; it is based on its wish to increase the services offered by retailers that sell Nine West products. We therefore grant Nine West's Petition on the basis that Nine West's use of resale price maintenance is not likely to harm consumers.").