No.

IN THE

Supreme Court of the United States

LEEGIN CREATIVE LEATHER PRODUCTS, INC.,

Petitioner,

v.

PSKS, INC., doing business as Kay's Kloset . . .
Kay's Shoes,

Respondent.

On Petition For A Writ Of Certiorari
To The United States Court Of Appeals
For The Fifth Circuit

PETITION FOR A WRIT OF CERTIORARI

TYLER A. BAKER
FENWICK & WEST, LLP
Silicon Valley Center
801 California Street
Mountain View, CA 94041
(650) 335-7624

THEODORE B. OLSON
Counsel of Record
MICHAEL L. DENGER
JOSHUA LIPTON
AMIR C. TAYRANI
GIBSON, DUNN & CRUTCHER LLP
1050 Connecticut Avenue, N.W.
Washington, D.C. 20036
(202) 955-8500

Counsel for Petitioner

[Additional Counsel Listed on Inside Cover]

JEFFREY S. LEVINGER
CARRINGTON, COLEMAN,
SLOMAN & BLUMENTHAL, LLP
901 Main Street
Suite 5500
Dallas, TX 75202
(214) 855-3000

GARY FREEDMAN
LAW OFFICES OF GARY FREEDMAN
1149 3rd Street, Suite 200
Santa Monica, CA 90403
(310) 576-2444

QUESTION PRESENTED

This Court has held that antitrust "*per se* rules are appropriate only for conduct that . . . would always or almost always tend to restrict competition." Modern economic analysis establishes that vertical minimum resale price maintenance does not meet this condition because the practice often has substantial competition-enhancing effects. The question presented is whether vertical minimum resale price maintenance agreements should be deemed *per se* illegal under Section 1 of the Sherman Act, or whether they should instead be evaluated under the rule of reason.

PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT

In addition to the parties named in the caption, Toni Cochran L.L.C., doing business as Toni's, was a plaintiff below.

Pursuant to this Court's Rule 29.6, undersigned counsel state that Leegin Creative Leather Products, Inc. is a wholly owned division of Brighton Collectibles, Inc. No publicly held company owns 10% or more of its stock.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner Leegin Creative Leather Products, Inc. ("Leegin") respectfully submits this petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit.

OPINIONS BELOW

The court of appeals' opinion is unpublished but electronically reported at 2006 WL 690946. App., *infra*, at 1a. The order denying Leegin's petitions for rehearing and for rehearing en banc is unreported. *Id.* at 16a. The opinion of the United States District Court for the Eastern District of Texas is unreported. *Id.* at 12a.

JURISDICTION

The district court had jurisdiction over respondent's claims pursuant to 28 U.S.C. § 1331. The court of appeals had jurisdiction to review the district court's final judgment pursuant to 28 U.S.C. § 1291. The court of appeals filed its opinion on March 20, 2006. It denied Leegin's timely petitions for rehearing and for rehearing en banc on July 19, 2006. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISION INVOLVED

Section 1 of the Sherman Act (15 U.S.C. § 1) provides, in pertinent part:

Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce . . . is hereby declared to be illegal.

STATEMENT

This case is an ideal vehicle for this Court to revisit its decision in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911), which relied upon the antiquated common-law rule against "restraints on alienation" to hold that a vertical agreement between a manufacturer and its retailers establishing minimum resale prices for the manufacturer's goods is a *per se* violation of the Sherman Act. *Id.* at 404. This *per se* rule—on which the Fifth Circuit relied in affirming the district court's judgment—squarely conflicts with accumulated economic knowledge, which recognizes that vertical minimum resale price maintenance can have significant *procompetitive* effects, and with this Court's modern antitrust jurisprudence, including decisions revisiting and rejecting analogous *per se* rules prohibiting other vertical agreements. *See State Oil Co. v. Khan*, 522 U.S. 3 (1997); *Cont'l T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977). As in *Khan* and *Sylvania*, the *per se* rule at issue here has been subject to overwhelming criticism and lacks support under the economic approach that this Court's recent antitrust jurisprudence has applied.

1. Leegin has built a successful family business in the crowded and intensely competitive marketplace for women's fashion accessories. In 1990, Leegin introduced the "Brighton" brand with a line of women's belts, and it later added other types of accessories to the Brighton line. Leegin has differentiated its products from the myriad other brands of leather goods and accessories available in department stores and mass merchandisers by focusing on boutique stores offering a level of service and personal attention that consumers often cannot find elsewhere. 6.R.5-11.[1]

Leegin's strategy has succeeded. Brighton has become a brand equated with quality, value, and customer service.

[1] "R" refers to the record on appeal. Citations to the record are to the volume of the record, followed by the page number in that volume.

Brighton products did not even exist until 1990, yet ten years later, despite competition from hundreds of other brands of women's accessories, Brighton products were sold in more than 5,000 specialty stores nationwide. 5.R.125-26; 6.R.17-20; 7.R.15. While Leegin has achieved impressive success from its humble beginnings, it is still a small company when compared to the much larger manufacturers and department stores with which it and its retailers compete. 3.R.813-20.

2. In 1997, Leegin instituted the "Brighton Retail Pricing and Promotion Policy," pursuant to which Leegin announced that it would do business exclusively with retailers who follow its suggested retail prices for Brighton products. 6.R.10.[2] There were two principal reasons for Leegin's adoption of the pricing policy. First, it was Leegin's view that the typical retail strategy of putting products on and off "sale" degrades a manufacturer's brand by causing customers to feel cheated when they buy at the wrong moment. 5.R.106-24. Leegin's policy instead furthered an "everyday fair price" approach. *Id.* Second, the pricing policy was designed to develop the Brighton brand by giving retailers incentives to provide special attention and service to Brighton customers. 5.R.115-27. In small specialty stores, attractive presentation and customer service are central to the shopping experience, but providing those services is not costless to retailers. *Id.* Through its pricing policy, Leegin ensured a sufficient margin to retailers to give them the incentive to focus on Brighton products and to provide high-quality service. *Id.*

Leegin's pricing policy was successful, and sales of Brighton products grew considerably after its inception. For example, sales of Brighton handbags increased from 125,609 units in 1996, to 375,480 units in 2003. *See* Expert Report of Kenneth G. Elzinga ("Elzinga Report") at 20 n.26 (App., *infra*, at 37a).

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[2] Leegin's pricing policy permitted retailers to discount products that they did not wish to re-order from Leegin.

3. Plaintiff PSKS, which operated a retail store known as "Kay's Kloset" in Lewisville, Texas, was one of the stores to which Leegin sold Brighton products. In December 2002, Leegin learned that PSKS was selling all Brighton products below the suggested prices, in violation of Leegin's pricing policy. 6.R.112-13. In response, Leegin suspended all shipments of Brighton products to PSKS. 6.R.118-19; 7.R.102-09. PSKS then filed this suit, alleging that Leegin's pricing policy constituted an unlawful agreement in restraint of trade.

The district court refused to allow Leegin to introduce evidence that its pricing policy promoted interbrand competition, and excluded the testimony of Leegin's economic expert, Professor Kenneth G. Elzinga. 1.R.325-33. Professor Elzinga would have testified, *inter alia*, that Leegin lacks market power and that its pricing practices are procompetitive because they foster interbrand competition. Elzinga Report at 5-20 (App., *infra*, at 22a-37a). The district court also denied Leegin's request for an instruction that would have allowed the jury to apply the rule of reason (1.R.190-92), which requires an antitrust plaintiff to demonstrate that the defendant's conduct unreasonably restrains competition in a relevant market before it will be found unlawful (*see Texaco Inc. v. Dagher*, 126 S. Ct. 1276, 1279 (2006)), and instead instructed the jury that the alleged resale price maintenance agreement is *per se* unlawful (11.R.42).

The jury found that Leegin's policy constituted a resale price maintenance agreement, and based on the verdict, the court awarded PSKS $3.6 million in damages and $375,000 in attorneys' fees. App., *infra*, at 3a. Leegin renewed its motion for judgment as a matter of law and moved in the alternative for a new trial. The court denied Leegin's motions, stating that "[w]hether the per se classification of such agreements is wise is not for this court to decide." *Id.* at 12a.

The Fifth Circuit affirmed the district court's decision, rejecting Leegin's request for rule-of-reason treatment because lower courts "remain bound by [the Supreme Court's]

holding in *Dr. Miles*." App., *infra*, at 4a. The Fifth Circuit called for a response to Leegin's petitions for rehearing and for rehearing en banc, but eventually denied the petitions.

After the Fifth Circuit refused to stay its mandate, Leegin applied to Justice Scalia for a stay pending the filing and disposition of a petition for a writ of certiorari. No. 06A179. Justice Scalia granted a temporary stay pending a response from PSKS. After a response was received, Justice Scalia referred the application to the Court, which granted the stay pending the filing and disposition of this petition.

REASONS FOR GRANTING THE PETITION

The *per se* rule against resale price maintenance squarely conflicts with this Court's modern antitrust jurisprudence, which has rejected *per se* treatment of analogous vertical agreements because such treatment lacked an economic justification. *See Sylvania*, 433 U.S. at 47-48 (rejecting the *per se* rule against vertical nonprice restraints, and explaining that the "great weight of scholarly opinion ha[d] been critical of the" rule); *Khan*, 522 U.S. at 18 (unanimously overturning the *per se* rule against vertical maximum price-fixing because there was "insufficient economic justification" for the rule); *see also Ill. Tool Works, Inc. v. Indep. Ink, Inc.*, 126 S. Ct. 1281, 1290-91 (2006) (unanimously overturning the presumption of *per se* illegality of a tying arrangement involving a patented product because it was inconsistent with economic analysis). Like the *per se* rules rejected in *Sylvania*, *Khan*, and *Independent Ink*, the rule of *Dr. Miles* has no foundation in economic theory because it is well-established that vertical minimum resale price maintenance agreements often have substantial procompetitive effects. The validity of such agreements is therefore more appropriately determined under the rule of reason, rather than through application of a rigid *per se* rule.

This Court "presumptively applies rule of reason analysis" to antitrust claims. *Dagher*, 126 S. Ct. at 1279. The Court has emphasized that a "departure from the rule-of-reason standard must be based upon demonstrable economic

effect." *Sylvania*, 433 U.S. at 58-59. The *per se* prohibition on resale price maintenance, however, rests upon outdated common-law notions that are inconsistent with economic theory and that were expressly rejected by this Court in *Sylvania* and *Khan*. Not surprisingly, legal and economic commentators have leveled sharp criticism at this *per se* rule, pointing out that it lacks any economic justification. For example, Judge Posner has described the *per se* rule against resale price maintenance as "a sad mistake," explaining that "[t]here is neither theoretical basis, nor empirical support, for thinking the practice generally anticompetitive." Richard A. Posner, *Antitrust Law* 189 (2d ed. 2001) [hereinafter Posner, *Antitrust Law*]. Numerous other commentators are in accord. *See, e.g.*, Thomas R. Overstreet, Jr., Bureau of Econ., Fed. Trade Comm'n, *Resale Price Maintenance: Economic Theories and Empirical Evidence* 164 (1983) ("the economic theories and the available empirical evidence rather clearly suggest that the rigid application of a strict standard of *per se* illegality for RPM [resale price maintenance] is inappropriate").

Moreover, because of its overbreadth, the rule of *Dr. Miles* inflicts substantial harm on competitive market processes. In particular, the rule proscribes conduct that, if permitted, would frequently be used for procompetitive purposes and would enhance consumer welfare. In this case, for example, Leegin is a small competitor that used resale price maintenance to provide incentives for retailers to market its products effectively against its larger rivals. The antitrust laws should promote, not condemn, a small manufacturer's efforts to expand its output through aggressive interbrand competition. The *per se* rule against resale price maintenance, however, undercuts this competitive tool and thus undermines interbrand competition—a result that is antithetical to the objectives of the antitrust laws.

This case, which is final in all respects, presents a singularly appropriate vehicle to reconsider the *per se* rule against resale price maintenance, which the Court has not squarely addressed under its modern antitrust jurisprudence. Review

by this Court is necessary to overturn this far-reaching and anachronistic *per se* rule and to bring the law of resale price maintenance into step with the law governing other vertical restraints.

I. THE RULE OF *DR. MILES* IS INCONSISTENT WITH THIS COURT'S MODERN ANTITRUST JURISPRUDENCE.

The *per se* rule against resale price maintenance is the lone remaining vestige of an antiquated antitrust regime that cannot be reconciled with either recent antitrust decisions or economic theory. This Court has abandoned the *per se* rules against other vertical arrangements—including vertical maximum price-fixing arrangements and all types of vertical nonprice restraints. Each of those other *per se* rules—like the rule of *Dr. Miles*—was based on the "ancient rule against restraints on alienation" (*United States v. Arnold, Schwinn & Co.*, 388 U.S. 365, 380 (1967)), which has no grounding in economics. And each of the other vertical *per se* rules was rejected when the Court applied an approach to antitrust analysis grounded in real-world economics. This Court should reexamine the rule of *Dr. Miles* to resolve the conflict between that outdated and overbroad *per se* rule and the Court's antitrust decisions of the last thirty years.

A. This Court Has Overturned Analogous *Per Se* Rules Against Other Vertical Agreements.

1. Nearly a century ago, this Court in *Dr. Miles* invalidated an agreement that required a manufacturer's dealers to abide by a minimum resale price. Without considering the competitive consequences of the practice, the Court held that these arrangements are invalid under the Sherman Act because such "restraints upon alienation have been generally regarded as obnoxious to public policy." *Dr. Miles*, 220 U.S. at 404. In his dissenting opinion, Justice Holmes rejected the majority's approach and argued that, in many circumstances, the public would "be served best by the company being al-

lowed to carry out its plan" to establish minimum resale prices. *Id.* at 412 (Holmes, J., dissenting).[3]

Following *Dr. Miles,* the Court adopted *per se* rules against other types of vertical restraints. In *Schwinn,* the Court held that vertical nonprice restraints, such as restrictions on the territories or customers that distributors may serve, are *per se* unlawful. 388 U.S. at 379-80. As in *Dr. Miles,* the Court based this *per se* rule on the "ancient rule against restraints on alienation," rather than on economic analysis. *Id.* at 380. The next year, the Court held that vertical maximum price restraints are *per se* unlawful, based on similar concerns for protecting dealer freedom. *See Albrecht v. Herald Co.*, 390 U.S. 145, 152 (1968).

When the Court had occasion to reexamine these *per se* rules in light of modern economic analysis, however, it determined that vertical agreements often have procompetitive effects and are therefore more appropriately evaluated on a case-by-case basis under the rule of reason. In *Sylvania,* for example, this Court overturned *Schwinn*'s *per se* rule against vertical nonprice restraints, and expressly rejected the notion that the common-law rule against restraints on alienation could justify a *per se* rule of antitrust liability. *Sylvania,* 433 U.S. at 53 n.21. The Court explained that "the state of the common law 400 or even 100 years ago is irrelevant to the issue before us: the effect of the antitrust laws upon vertical distributional restraints in the American economy today." *Id.* (internal quotation marks omitted). Instead, "[*p*]*er se* rules of illegality are appropriate only when they relate to conduct that is manifestly anticompetitive." *Id.* at 49-50. The Court further explained that *per se* analysis is ill-suited to vertical restrictions "because of their potential for a simultaneous re-

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[3] *See also id.* ("I cannot believe that in the long run the public will profit by this court permitting knaves to cut reasonable prices for some ulterior purpose of their own and thus to impair, if not to destroy, the production and sale of articles which it is assumed to be desirable that the public should be able to get.").

duction of intrabrand competition and stimulation of interbrand competition." *Id.* at 51-52. In light of this potential for procompetitive effects, the Court concluded that the validity of vertical nonprice restraints should be determined under the rule of reason. *Id.* at 58.

Similarly, in *Khan*, this Court unanimously overruled its holding in *Albrecht* that vertical maximum price restraints are *per se* unlawful. As in *Sylvania*, the Court explained that concerns with "dealer freedom" are not an appropriate basis for a *per se* rule of antitrust liability. *Khan*, 522 U.S. at 16-17. Instead, the Court held that *per se* treatment is only "appropriate once experience with a particular kind of restraint enables the Court to predict with confidence that the rule of reason will condemn it." *Id.* at 10 (internal quotation marks omitted). Building on the critiques of *Albrecht* offered by lower courts and commentators, the Court concluded that the *per se* rule should be rejected because there is "insufficient economic justification for *per se*" treatment of vertical maximum price restraints. *Id.* at 18.

2. The reasoning of this Court's decisions in *Sylvania* and *Khan* severely undermines the rule of *Dr. Miles*. The Court's focus, nearly a century ago, on "restraints on alienation" is no longer a valid basis for a *per se* rule of antitrust law. Instead, a *per se* rule is appropriate *only* for "conduct that would always or almost always tend to restrict competition and decrease output." *Bus. Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 723 (1988) (internal quotation marks omitted).

This Court has identified certain prerequisites to application of a *per se* rule in the antitrust context. First, a "departure from the rule-of-reason standard must be based upon demonstrable economic effect rather than . . . upon formalistic line drawing." *Sylvania*, 433 U.S. at 58-59; *see also Sharp*, 485 U.S. at 724. Second, *per se* treatment is appropriate only when "experience with a particular kind of restraint enables the Court to predict with confidence that the rule of reason will condemn it." *Khan*, 522 U.S. at 10 (inter-

nal quotation marks omitted). The Court has thus "expressed reluctance to adopt *per se* rules with regard to 'restraints imposed in the context of business relationships where the economic impact of certain practices is not immediately obvious.'" *Id.* (quoting *FTC v. Ind. Fed'n of Dentists*, 476 U.S. 447, 458-59 (1986)). As discussed below, the *per se* rule of *Dr. Miles* satisfies neither of these criteria.

B. There Are No Demonstrable Economic Effects That Support *Per Se* Treatment Of Resale Price Maintenance.

In both *Sylvania* and *Khan*, this Court examined the economic effects of the vertical restraints at issue, including by considering "scholarly and judicial authority supporting their economic utility." *Sylvania*, 433 U.S. at 57-58; *see also Khan*, 522 U.S. at 15-19. Based on that examination, the Court found "insufficient economic justification" for *per se* treatment of vertical nonprice and vertical maximum price restraints. *Khan*, 522 U.S. at 18; *see also Sylvania*, 433 U.S. at 57-58. The same result is required in the context of resale price maintenance. Indeed, economic and legal scholars have reached an unusually strong consensus in support of the conclusion that resale price maintenance has a number of procompetitive uses and effects that, if permitted by the antitrust laws, could enhance consumer welfare. *See, e.g.*, ABA Antitrust Section, *Antitrust Law and Economics of Product Distribution* 76 (2006) (the "bulk of the economic literature on RPM . . . suggests that RPM is more likely to be used to enhance efficiency than for anticompetitive purposes").[4]

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[4] *See also* 8 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 1611 (2d ed. 2004); Robert H. Bork, *The Antitrust Paradox* 289 (1978); Kenneth G. Elzinga & David E. Mills, *The Economics of Resale Price Maintenance* 1-5, *at* http://www.virginia.edu/economics/papers/mills/RPM%20for%20ABA.pdf (forthcoming 2007); Posner, *Antitrust Law*, *supra*, at 172; David A. Butz, *Vertical Price Controls with Uncertain Demand*, 40 J.L. & Econ. 433, 455-57 (1997); Ralph A. Winter, *Vertical Control and Price Versus Nonprice Competition*, 108 Q.J. Econ. 61, 72

1. Vertical Price And Nonprice Restraints Often Have Procompetitive Effects On Interbrand Competition.

A simplistic—and incorrect—criticism of vertical restrictions (including both price and nonprice restraints) is that they limit intrabrand price competition, raise retailers' margins, often raise retail prices, and are therefore harmful to consumers. That analysis, however, is wrong as a matter of economics and inconsistent with this Court's analysis of vertical restraints.

In *Sylvania*, the Court recognized that manufacturers often use vertical restraints to create incentives for their dealers to provide service and promote the manufacturer's product, which, in turn, fosters interbrand competition:

> Vertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of his products. . . . Economists have identified a number of ways in which manufacturers can use such restrictions to compete more effectively against other manufacturers. For example, new manufacturers and manufacturers entering new markets can use the restrictions in order to induce 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. Established manufacturers can use them to induce retailers to engage in promotional activities or to provide ser-

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[Footnote continued from previous page]

(1993); Andrew N. Kleit, *Efficiencies Without Economists: The Early Years of Resale Price Maintenance*, 59 S. Econ. J. 597, 617 (1993); Frank H. Easterbrook, *Antitrust Law Enforcement in the Vertical Restraints Area: Vertical Arrangements and the Rule of Reason*, 53 Antitrust L.J. 135, 146-48 (1984); Overstreet, *supra*, at 11.

> vice and repair facilities necessary to the efficient marketing of their products.

433 U.S. at 54-55 (citation and footnote omitted). As the Court noted, "these services might not be provided by retailers in a purely competitive situation" because of "market imperfections such as the so-called 'free rider' effect." *Id.* at 55.

In *Sharp*, the Court emphasized that "vertical nonprice restraints only accomplish the benefits" to interbrand competition identified in *Sylvania* "*because they reduce intrabrand price competition* to the point where the dealer's profit margin permits provision of the desired services." *Sharp*, 485 U.S. at 728 (emphasis added). And, as the Court stated in *Sylvania*, interbrand competition is the "primary concern of antitrust law." 433 U.S. at 52 n.19; *see also* Bork, *supra*, at 290; Overstreet, *supra*, at 48.

Moreover, as this Court explained in *Sylvania*, a manufacturer has no interest in overcompensating its retailers by enabling fat retail margins—to the contrary, "a manufacturer would prefer the lowest retail price possible, once its price to dealers has been set, because a lower retail price means increased sales and higher manufacturer revenues." 433 U.S. at 56 n.24. Accordingly, "manufacturers have an economic interest in maintaining as much intrabrand competition as is consistent with the efficient distribution of their products." *Id.* at 56; *see also* Bork, *supra*, at 290 ("No manufacturer or supplier will ever use either resale price maintenance or reseller market division for the purpose of giving the resellers a greater-than-competitive return. . . . The manufacturer shares with the consumer the desire to have distribution done at the lowest possible cost consistent with effectiveness.").

Notably, a manufacturer uses many tools to enhance its interbrand competitive position that might increase nominal

prices to consumers.[5] Manufacturers may engage in national advertising or upgrade their product features, the costs of which get passed through to consumers in the form of increased prices—yet no one would argue that this conduct in a competitive marketplace is an anticompetitive activity. *See* Elzinga & Mills, *supra*, at 8-9; Easterbrook, *supra*, at 141. The presence of *inter*brand competition assures that manufacturers' actions to promote their products—including vertical distribution restraints—are geared toward efficiency and procompetitive results. *Sylvania*, 433 U.S. at 52 n.19, 56 n.24. If the manufacturer takes actions that boost prices without promotional benefits that consumers desire, it will lose sales to its interbrand competitors. *Id.*; Overstreet, *supra*, at 48. On the other hand, if the manufacturer's sales increase because consumers are getting more services that they value, then consumers benefit. Elzinga & Mills, *supra*, at 9.

Vertical price and nonprice restraints can both be used to enhance interbrand competition in this manner. Indeed, "there is a substantial body of economic analysis supporting the view that the distinction" between vertical price and nonprice restraints "is largely illusory." ABA Antitrust Section, *supra*, at 59; *see also Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 762 (1984) ("the economic effect" of "price and nonprice restrictions" is in many cases "similar or identical"). As Justice White explained in his concurrence in *Sylvania*, "[i]t is common ground among the leading advocates of a purely economic approach to the question of distribution restraints that the economic arguments in favor of al-

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[5] While the use of resale price maintenance may lead to higher nominal retail prices, empirical analysis has shown that the practice can, in some situations, actually result in *lower* retail prices, in addition to the proconsumer benefits of increased services stimulated by the practice. *See* Overstreet, *supra*, at 138-40. For example, if resale price maintenance allows a manufacturer to compete more effectively and thereby expand its sales and output, the manufacturer may achieve efficiencies in manufacturing or distribution that could allow it to lower its unit costs and prices. *See id.* at 47-48.

lowing vertical nonprice restraints generally apply to vertical price restraints as well." 433 U.S. at 69 (White, J., concurring). Indeed, the procompetitive uses of vertical territorial restraints to reduce intrabrand price competition identified by this Court in *Sylvania* and *Sharp* as supporting rule-of-reason treatment are equally applicable to resale price maintenance. *Id.* at 69-70; Posner, *Antitrust Law*, *supra*, at 184 ("any argument for the legitimacy of exclusive territories applies equally to resale price maintenance").

It is thus untenable that resale price maintenance should continue to be treated under a vastly different legal standard than all other vertical restraints. As Judge Bork wrote, "This field of law can be made clear, internally consistent, and congruent with reality only when we face the fact that the premise laid down in *Dr. Miles* . . . is incorrect and must be rejected." Bork, *supra*, at 298. The divergence in treatment of these similar vertical restraints, standing alone, is a strong reason for the Court to reexamine the rule of *Dr. Miles*.

2. There Are Many Uses Of Resale Price Maintenance That Can Enhance Interbrand Competition And Consumer Welfare.

It is well-accepted among legal and economic scholars that resale price maintenance, if permitted by the antitrust laws, would frequently be used for procompetitive purposes, such as providing incentives to retailers to stock and promote the manufacturer's products. *See, e.g.*, Frank Mathewson & Ralph Winter, *The Law and Economics of Resale Price Maintenance*, 13 Rev. Indus. Org. 57, 81 (1998) ("[P]rice floor restraints are used in most cases unilaterally by a manufacturer to change the mix of price and non-price competition among retailers of its product. Restrictions on distribution are a means of competing on product quality."). "[N]o single specific theory explains all instances of [resale price maintenance]"—instead, there are a number of different purposes for which a manufacturer might implement resale price maintenance that are likely to have procompetitive virtues and en-

hance consumer welfare. Winter, *supra*, at 70. The common thread among these uses is that the manufacturer provides its retailers with a guaranteed margin as a means to enhance its competitive position against interbrand rivals.

The most commonly cited justification for resale price maintenance is that a manufacturer might impose a price floor to ensure that dealers provide demand-creating services. *See, e.g.*, Elzinga & Mills, *supra*, at 3; Overstreet, *supra*, at 49; Lester G. Telser, *Why Should Manufacturers Want Fair Trade?*, 3 J.L. & Econ. 86, 91 (1960). In the absence of resale price restraints, free-rider problems may diminish retailers' incentives to provide these services, harming the manufacturer and dampening interbrand competition. *See, e.g.*, Posner, *Antitrust Law*, *supra*, at 173.

Even outside the classic free-rider situation, resale price maintenance may be used by a manufacturer to provide its retailers with incentives to compete on service, where the retailer might otherwise have an inherent bias to rely too much on low prices (and not enough on service or promotional activities) to attract customers, which could reduce the manufacturer's overall interbrand competitive position. *See* Winter, *supra*, at 62-64. While a manufacturer might theoretically contract with its retailers to provide certain services, the transaction and monitoring costs associated with such a program can be prohibitive, and it can be far more efficient for a manufacturer to encourage retailers to compete on service by limiting intrabrand price competition. *Id.*

A manufacturer may also use resale price maintenance to encourage retailers to stock its products by guaranteeing a minimum resale margin, essentially "purchas[ing] shelf space in higher cost retail outlets." Overstreet, *supra*, at 47. The ability to "purchase" shelf space through resale price maintenance can be particularly important for a new or small manufacturer trying to break into the marketplace. *See, e.g.*, Mathewson & Winter, *supra*, at 60 ("In markets where extensive distribution systems are necessary, RPM is often used in the early part of a product's life cycle to aid in the estab-

lishment of the distribution system. In this situation, . . . RPM lowers the barriers of entry into upstream markets.").

Similarly, a manufacturer may use resale price maintenance to encourage its retailers to purchase more of its products, particularly in industries in which excess inventory can be subject to heavy discounting (such as the women's fashion industry, in which Leegin competes). Resale price maintenance ensures that retailers will be protected from a dramatic devaluation of their inventory when demand is unexpectedly low and, consequently, it reduces the chance that risk-averse retailers will purchase too little out of concern for having unsold stockpiles at the end of the season. *See, e.g.*, Butz, *supra*, at 451-52. A manufacturer, in turn, might use resale price maintenance to expand output or introduce more innovative products because retailers would be more willing to carry its products, enhancing interbrand competition and benefiting consumers. *Id.* at 457.

3. The Possibility That Resale Price Maintenance Might Be Used By A Cartel Does Not Justify The Rule Of *Dr. Miles.*

Of course, not every use of resale price maintenance is necessarily procompetitive. It is possible, for example, that resale price maintenance (just like vertical territorial restraints) might be used to enforce a horizontal agreement among dealers or manufacturers. *See* Posner, *Antitrust Law*, *supra*, at 183-85. The conditions in which such a cartel might theoretically operate, however, are extremely rare. Elzinga & Mills, *supra*, at 5-6; Easterbrook, *supra*, at 141-43. And, as demonstrated by empirical studies, instances of resale price maintenance being used for procompetitive purposes are "far more common" than instances in which it is used to facilitate a cartel. Pauline M. Ippolito, *Resale Price Maintenance: Empirical Evidence from Litigation*, 34 J.L. & Econ. 263, 282 (1991); *see also* Overstreet, *supra*, at 162 (empirical evidence "suggests that neither supplier nor dealer collusion explanations are likely to apply to all or even most instances of price maintenance").

There is neither an empirical nor a theoretical basis to conclude that consumers or competition benefit from a ban on *all* uses of resale price maintenance out of a concern over potential collusive uses of the practice, which could only exist under specific and uncommon market conditions. To the contrary, the empirical evidence "suggest[s] that, on the margin, the dominant effect of a relaxation of the per se prohibition of RPM would be a reduction in the deterrence of non-collusive uses of RPM." Ippolito, *supra*, at 292. Moreover, this Court's precedents do not support applying a *per se* rule that ensnares substantial procompetitive conduct simply out of fear of occasional anticompetitive uses. As discussed above, *per se* rules are appropriate *only* where a practice always, or almost always, results in anticompetitive effects. *See Sharp*, 485 U.S. at 723; Easterbrook, *supra*, at 142-43.

In any event, there is no reason to believe that the existing *per se* rules against horizontal collusion and the methods of detecting and punishing such collusion are so lacking as to justify additional *per se* rules as a prophylactic measure to bolster cartel enforcement. This Court addressed a similar issue in *Sylvania*, in which it noted that "[t]here may be occasional problems in differentiating vertical restrictions from horizontal restrictions originating in agreements among the retailers." 433 U.S. at 58 n.28. The Court concluded, however, that "we do not regard the problems of proof as sufficiently great to justify a *per se* rule." *Id.* The same reasoning requires rejection of the argument that a fear of cartels can support a *per se* rule against vertical price restraints.

4. Leegin Used Resale Price Maintenance For Procompetitive Purposes.

The facts of this case powerfully illustrate the competition-enhancing potential of resale price maintenance. Indeed, there is no allegation, evidence at trial, or even a realistic possibility that Leegin's conduct was part of a collusive horizontal scheme. *See* Elzinga Report at 14-18 (App., *infra*, at 31a-35a). There is also no evidence or suggestion that Leegin had market power. To the contrary, Leegin is but a

small player in the fragmented and highly competitive marketplace for women's fashion accessories. *Id.* at 16-20 (App., *infra*, at 33a-37a). In these circumstances, there is no realistic possibility that Leegin's use of resale price maintenance could harm consumers. *See id.* at 26-27 (App., *infra*, at 43a-44a).

Leegin used resale price maintenance in an attempt to bring new products and services to consumers and to use small retailers to compete against prominent national brands sold through department stores and other large outlets. *See* Elzinga Report at 10-12 (App., *infra*, at 27a-29a). This case presents precisely the circumstances in which resale price maintenance can *enhance* interbrand competition and consumer welfare. Indeed, the fact that Leegin's output grew substantially while its pricing policy was in effect indicates strongly that competition was enhanced and that consumers have benefited from the policy. *Id.* at 20 (App., *infra*, at 37a); *see also* Richard A. Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. Chi. L. Rev. 6, 21 (1981) ("If [the defendant's] output expanded, the restriction must have made the firm's product more attractive on balance, thereby enabling the firm to take business from its competitors. This is an increase in interbrand competition and hence in consumer welfare, which is the desired result of competition."); Easterbrook, *supra*, at 163-64. Holding Leegin's conduct to be *per se* unlawful stifles the competitive behavior of a small and innovative company, and thus conflicts with the objectives that this Court has sought to promote in interpreting the antitrust laws.

C. There Is No Judicial Experience With Resale Price Maintenance That Could Enable The Court To Predict With Confidence That The Rule Of Reason Will Condemn It.

This Court has often repeated that a *per se* rule is only appropriate "once experience with a particular kind of restraint enables the Court to predict with confidence that the rule of reason will condemn it." *Khan*, 522 U.S. at 10 (inter-