

IP ADVISOR

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2007 ISSUE**U.S. SUPREME COURT ENDS *PER SE* ILLEGALITY OF MINIMUM RESALE PRICE
HOLDERS OF MAINTENANCE AGREEMENTS, MANUFACTURERS AND LICENSORS
SHOULD HAVE CAUTIOUS OPTIMISM***By Gregory S. William*

In *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 551 U.S. ____ (2007), the U.S. Supreme Court made it easier for manufacturers and licensors to set the minimum price at which their goods can be sold. This practice, commonly known as minimum resale price maintenance (“RPM”) had long been considered *per se* (automatically) illegal under a nearly century-old line of court decisions. This article will explain the potential effects of the decision on intellectual property owners, what the decision means, and, just as importantly, what the decision does *not* mean.

RPM and IP Owners

The most obvious impact of the *Leegin* decision involves the ability of manufacturers and licensors to set minimum prices for their goods, as discussed below. With licensing of IP an ever-increasing source of revenue for many companies, licensors may now be able to agree not only on royalties to be paid by a licensee, but also on the minimum price at which the products embodying the IP are to be sold. Additionally, trademark owners may now be better able to control the connotation their mark gives to consumers, particularly in the case of luxury goods, through setting the minimum price at which the goods bearing the trademark are sold. To better understand how the antitrust landscape has changed, a brief look at antitrust law and the *Leegin* case is useful.

The History of RPM and the *Leegin* Case**1. A Primer on Antitrust Law**

Section 1 of the Sherman Act prohibits every “contract, combination and conspiracy in restraint of trade.” Many antitrust cases have focused on determining what exactly constitutes a “restraint of trade.” The goal of antitrust law is to promote competition, which is ultimately thought to benefit consumers. While violations of Section 1 were originally considered *per se* illegal, the modern trend for most cases is to look at the potentially illegal action, compare the potential procompetitive and anticompetitive effects of the action, and then determine whether the action tends to mainly restrain or promote competition. Several factors are instrumental in this analysis, including the market power of the parties to the agreement.

This analysis, utilizing modern economics, is commonly referred to as the “Rule of Reason” (“ROR”). The ROR looks at the expected and actual effects of an action on the marketplace, rather than analyze the possible effects in a vacuum. In looking at an action that may potentially harm competition, another key aspect is whether the action affects intrabrand competition, such as competing retailers that sell the goods of the same manufacturer, or interbrand competition, such as competing manufacturers of similar goods. Agreements that affect intrabrand competition are commonly referred to as

“vertical restraints,” while agreements that affect interbrand competition are often called “horizontal restraints.” RPM falls into the category of vertical restraints, as it involves agreements between manufacturers/licensors and their distribution/sales chains or licensees.

2. The Leegin Case

In *Leegin*, the plaintiff was a designer, manufacturer and distributor of leather goods and accessories. Leegin sold its goods mostly through small, independent retailers. PSKS operated one of these retailers, named “Kay’s Closet,” (“Kay’s”) and Leegin’s products constituted a large portion of Kay’s sales. Leegin instituted a “retail pricing and promotion policy,” and Leegin refused to sell to retailers that sold certain Leegin goods below the suggested prices. When Leegin discovered that Kay’s and other retailers were selling below the suggested prices, Leegin requested that Kay’s stop discounting. When Kay’s refused, Leegin ceased selling to Kay’s, and, after Kay’s sales revenue drastically declined, Kay’s brought suit.

At the time of the *Leegin* case, most other vertical restraints, including agreements to set *maximum* resale prices, were already being judged under the less restrictive ROR, a fact not lost on the Court in *Leegin*. Furthermore, as the *per se* rule does not allow a defendant the chance to offer evidence of procompetitive effects of the alleged restraint, the Court stated that a *per se* rule should only be used where courts have significant experience with a particular practice, and have found that the practice almost always has anticompetitive effects. Finally, the Court found that besides possible anticompetitive effects, RPM can have several important procompetitive ones. Some examples provided include preventing “free riding” by a discounter on retailers that spend large amounts of money promoting interest in a product, and giving new manufacturers the ability to induce competent and aggressive retailers to sell their goods.

What Does It Mean?

Post *Leegin*, the opportunity exists for manufacturers to implement a successful minimum RPM program, which, in the view of the Supreme Court, can benefit manufacturers, retailers and consumers alike. Besides the potential benefits discussed above, the Court in *Leegin* believed such agreements can alleviate competition between retailers of the same brand, based on price. This allows retailers to focus on other means of competition, such as better service and advertising. The belief is better service and advertising lead to happier and more educated customers. In turn, happier customers lead to increased sales; something in the interest of both manufacturers and retailers.

What Does It NOT Mean?

It is important to realize that the *Leegin* decision did not make minimum RPM *per se* legal, it just made it no longer *per se* illegal. Furthermore, the decision does not affect existing prohibitions against horizontal price-fixing agreements between competitors. These agreements continue to be considered *per se* illegal. A vertical minimum retail price agreement can still be held illegal under “Rule of Reason” analysis; the decision in *Leegin* just makes it harder for a plaintiff to prove its case. Indeed, the Court stated that if the ROR were to apply to minimum retail price maintenance programs, which it now does, “[C]ourts would have to be diligent in eliminating their anticompetitive uses from the market.” While the decision creates the possibility of a legal and successful minimum RPM agreement, any licensor or manufacturer thinking of implementing such a program should first recognize the potential liabilities, and carefully balance them

against the potential benefits. Moreover, in crafting such an agreement, it should be remembered that the agreement must have arguably procompetitive justifications, if the agreement is to have a chance at withstanding a Sherman Act, Section 1 challenge.

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