

Resale Price Maintenance and Consumer Welfare

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The basic issue in this exchange¹ is whether Professors Gould and Yamey have materially weakened the case I made for the legality of resale price maintenance (r.p.m.) desired by a manufacturer who is not in collusion with other manufacturers.² I believe they have not. In this response I will try to demonstrate that their Rejoinder's strictures on welfare economics are irrelevant, its price theory mistaken, and its demands for certainty one-sided and unreasonable.

I. Welfare Economics

My position is that consumer welfare is the only proper criterion for antitrust generally and, specifically, for deciding the legality of r.p.m. I argued this position primarily within the context of judge-made rules under antitrust laws structured like those of the United States,³ but I am quite willing to follow Professors Gould and Yamey into the wider context of legislative decision-making. Discussing both legislatures and courts, Gould and Yamey quite correctly state that "we must distinguish two areas in which the criteria are to apply: (1) in the formulation of antitrust policy; and (2) in supplying the courts (or other implementing agency) with operational rules."⁴ I will make that distinction explicit in the discussion that follows since it is crucial to legitimate government that the division of functions between the two institutions be observed. Whether the legislature or the courts take up the problem of r.p.m., however, I believe r.p.m. of the type under discussion⁵ should be made lawful.

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1. The relevant prior pieces in the exchange are Bork, *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division I*, 74 YALE L.J. 775 (1965), and *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division II*, 75 YALE L.J. 373 (1966) [hereinafter cited as *Part I* and *Part II*, respectively]; Gould and Yamey, *Professor Bork on Vertical Price Fixing*, 76 YALE L.J. 722 (1967), and Bork, *A Reply to Professors Gould and Yamey*, 76 YALE L.J. 731 (1967) [hereinafter cited as *Reply*].

2. Professors Gould and Yamey seek, through a disavowal of "any policy prescription," to avoid the burden of sustaining a position of their own. I find the disavowal unpersuasive, and not merely because of the tone of their pieces and the prior writings of Professor Yamey. See, e.g., B. S. YAMEY, *THE ECONOMICS OF RESALE MAINTENANCE* (1954), especially at 129-30. If their "presumption" against r.p.m. is not a "policy prescription," it certainly bears a remarkable family resemblance to one.

3. See Bork, *Part I*, 74 YALE L.J. 775, 829 et seq. (1965), and Bork, *Reply*, 76 YALE L.J. 731, 740-41 (1967).

4. Gould and Yamey, *Professor Bork on Vertical Price Fixing: A Rejoinder*, 77 YALE L.J. 936, 945 (1968) [hereinafter cited as *Rejoinder*].

5. The reader is reminded that we are debating the desirability from the consumer's

A. *The Standard Welfare Analysis*

I proceed on the conventional hypothesis that antitrust is concerned with competition because a competitive regime provides society with the maximum output that can be achieved at a given time with the resources available. For the sake of clarity, it may be worth restating in simplified form the arguments that underlie this hypothesis.

Under a competitive regime each productive resource tends to move to that employment in which the value of its marginal product, and hence the return paid to it, is greatest. Output is then maximized because there is no possible rearrangement of resources that could increase consumer want satisfaction. Though changing wants and technologies prevent the attainment of this equilibrium, competition permits the closest approximation at any given moment and the continual pursuit of the shifting equilibrium point.

Monopolies (including cartels) interfere with this situation because the unified industry maximizes its net returns by keeping its output below the level which would be attained under a competitive structure. The resulting divergence between price and marginal cost means that the values of the marginal products of the resources employed by the monopolist are higher than they are in competitive industries. Consumers would be better off if resources moved from competitive industries to the presently monopolized industry until the values of marginal products were the same everywhere.

This model does not imply that change is undesirable. As producers achieve greater efficiency in resource use, the society becomes richer. A consumer-oriented antitrust law, therefore, should permit those market structures, agreements, and acts which reflect or create efficiency while prohibiting those which create restrictions of output.⁶

R.p.m. does not eliminate any competition at the manufacturing level and therefore cannot introduce or enlarge any ability to restrict output there. As I have attempted to show in prior pieces, r.p.m. cannot be expected to restrict output at the reseller level for the simple reason that no sane manufacturer would use it if that were its net effect. A

viewpoint of vertical price fixing, that is, r.p.m. which is not the tool of a cartel among resellers or among manufacturers. Hereafter references to "r.p.m." should be taken to indicate only this variety.

6. Though this statement will suffice for the purposes at hand, it is oversimplified. It is possible that movement from a condition in which marginal cost and price were equal to one in which they diverged would, nonetheless, be beneficial to consumers. A monopolistic merger, for example, would be preferable to the maintenance of a competitive structure if it created efficiencies which outweighed the restriction of output. Antitrust, however, does not try to measure directly the relative influences of restriction of output and efficiency in particular situations, but wisely settles for general rules. These rules should, of course, be based upon the probable effects of phenomena of various types.

manufacturer will want r.p.m. only if it increases reseller efficiency in distributing his product, and my prior pieces specified the ways in which r.p.m. can enhance distributive efficiency. It follows from these considerations and the model of welfare analysis sketched out above that r.p.m. desired by a manufacturer should be lawful. I turn now to those objections raised by Gould and Yamey which consist of efforts to show that my welfare criteria are inadequate. These objections have primarily to do with the theory of second best, income distribution, changes in consumer tastes, and the output criterion.

B. *The Theory of Second Best*

Gould and Yamey and I appear to be in agreement that the theory of second best does not provide criteria usable by courts in the decision of individual antitrust cases. It follows, and this seems not in dispute, that any consideration of second best must be at the level of overall rule-making.⁷ We may turn, then, to ask whether the theory of second best provides any guidance to the legislature (or to a court free to act legislatively) in the formulation of rules about r.p.m.

The theory of second best, as Gould and Yamey summarize it, states that so long as there are invulnerable monopolies in an economic system, it may or may not be worthwhile to attack and destroy those monopolies which are vulnerable. The reason is that if we attack vulnerable monopoly *A*, thereby equalizing the value of the marginal products as between *A* and competitive industries, the factors required for *A*'s expansion of output may have come from invulnerable monopoly *B* where their marginal products were higher. We have, if that should be the case, done consumers a disservice.

Gould and Yamey have stated the theory as a caution against assuming that a public policy against restrictions of output necessarily benefits consumers. Whatever weight one assigns to that caution, it clearly does not apply to my contention, grounded in basic price theory, that r.p.m. creates efficient utilization of resources. It is theoretically possible that the more efficient utilization of resources within a firm or an industry might shift demand or resources in such a way as to lessen consumer welfare, but our centuries-long experience of in-

7. The theory of second best, therefore, does not alter the tasks, and should not affect the analysis, of courts charged with applying the Sherman Act to r.p.m. I have argued that the Sherman Act must, for reasons intrinsic to the judicial process, be taken to rest upon standard consumer welfare concepts which are applied through criteria provided by price theory. Bork, *Part I*, 74 *YALE L.J.* 775, 829-47 (1965). I have also contended that this result is indicated by the legislative history of the statute. Bork, *Legislative Intent and the Policy of the Sherman Act*, 9 *J. LAW & ECON.* 7 (1966).

creases in wealth associated with changes in processes and techniques and the alteration of products certainly indicates that such results are improbable. No legislature would be justified in framing a rule against cost-cutting improvements or alterations in the composition of products because of speculations of this sort. Unless r.p.m. is shown to be different from other methods of improving distributive efficiency or changing product composition there is no warrant for raising the theory of second best in this discussion.

Gould and Yamey have in fact introduced a theory which, if taken seriously, undercuts the significance of their conclusions drawn from price theory, not mine. They contend r.p.m. may restrict output within an industry, but second best suggests that restrictions may not be an objection from a welfare standpoint. I do not press this latter point against them since I have doubts about the probability of the result which second best merely shows to be possible.⁸

The theory of second best, therefore, does not alter the appropriate welfare criteria if my price theory is correct. If it is not, I have no wish to take advantage of the escape hatch second best might provide. Second best thus has no relevance to this discussion.

C. *Income Distribution*

Gould and Yamey apparently suggest that, once the theory of second best has eliminated the criterion of consumer welfare, a legislature may properly rely upon the concept of income distribution to decide

8. For the sake of completeness, let us assume *arguendo* that r.p.m. does usually restrict output. What then is the relevance of the theory of second best? The legislature may make one of three possible assumptions about the impact of second best upon standard welfare analysis. If the theory leaves the legislature convinced that the best general rule is still that of standard welfare analysis, r.p.m. should be illegal. If the legislature thinks the theory suggests a reversal of the rule derived from standard welfare analysis, which I believe no one really suggests, output-restricting r.p.m. should be lawful. If the legislature concludes that the proper counsel of the theory of second best is complete agnosticism concerning the effects of restrictions of output on consumer welfare, and this seems to be the assumption upon which Gould and Yamey operate, then, of course, the interests of consumers drop entirely out of the policy equation. We now have a situation in which the only relevant parties are a manufacturer who does not wish to deal except upon a certain contractual term and at least one reseller who wishes to deal without agreeing to that term. The issue then is whether the state shall leave the parties free to make whatever bargain they can or shall intervene to say the demanded term is illegal because one of the parties would prefer to be relieved of it. I have no doubt that the state should leave the parties free and should enforce the term if it is ultimately incorporated in the bargain. This conclusion rests upon a general presumption in favor of freedom of contract where, as here, there is nothing which can realistically be termed force, fraud, or mistake, and where, by definition in this situation, the interests of third parties are not knowable and hence not weighed. Thus, the only case in which r.p.m. should be unlawful is where second best is regarded as too insubstantial to modify standard welfare analysis and where r.p.m. restricts output. Since I have agreed to these criteria from the beginning, consideration of second best has altered nothing.

the legality of r.p.m. I have shown that the necessary condition to this argument does not exist because the theory of second best does not question the value to consumers of r.p.m. which creates efficiency. Consumer welfare remains a usable criterion for judging r.p.m., therefore, and the field is not cleared for income distribution to assume the role of the decisive criterion by default. In this section, however, I will go further and attempt to demonstrate that the concept of income distribution should not, in any event, play any part in deciding the desirability of r.p.m. It is a subject to be considered after the legality of r.p.m. has been decided on other grounds.

Concern about income distribution may arise either because of a general policy with respect to the acceptable overall range of income disparities in a society or because the society wishes to take away income derived from a particular practice which it wishes to inhibit. The first cause for concern about income distribution tells us nothing about the desirability of r.p.m. A court has no business determining the range of acceptable income disparities in a society and, if it did, would have no reason to select the prohibition of r.p.m. as its means of controlling the disparities. The legislature, worried about the general problem of disparities, has at hand general remedies, such as taxation, subsidization, and welfare programs to achieve its ends. A general incomes policy, in itself, suggests nothing about particular income-producing activities. On such grounds r.p.m. is indistinguishable amidst an infinite range of such activities.

But I suspect Gould and Yamey are focusing on r.p.m. as a practice to be inhibited because of its particular effects. This interpretation of their remarks is reinforced by their reference to the award of damages to a "wronged party" and the footnote which apparently suggests theft and forgery as analogies.⁹ The fallacy here lies in the assumption that the policy-making body usually selects those acts which are to be made illegal or for which damages may be claimed according to some standard of income distribution. Income distribution, by itself, does not distinguish between "fencing" stolen goods and normal brokering as means of gaining income. Theft and forgery, to take Gould and Yamey's examples, are not defined as wrongs because they alter income distribution but because they have other effects which are regarded as deleterious. If r.p.m. creates efficiency and so increases society's wealth, there is no more reason for a legislature to classify it as an undesirable practice, analogous to a tort or crime, than there is to clas-

9. Gould and Yamey, *Rejoinder*, 77 YALE L.J. 936, 947 & n.22 (1968).

sify the more efficient rearrangement of machinery as a thing wrong in itself simply because it produces income. If r.p.m. restricts output, it injures consumers and may properly be made illegal. The subject of income distribution then becomes relevant for the first time and may suggest a provision for the recovery of damages as a way of preventing men from deriving income from antisocial conduct.

Thus, price theory, which indicates the effect of r.p.m. on resource allocation, and welfare analysis, which indicates the effect of resource allocation upon consumers, control the decision as to the desirability of r.p.m.¹⁰ The subject of income distribution becomes relevant only after that decision is made. Hence the topic has no relevance to the present discussion.

D. *Changes in Taste*

Professors Gould and Yamey offer an argument which amounts to no more than this: "Bork has relied on standard welfare analysis. He is, for that reason, confined to policy prescriptions which can be derived rigorously and with certainty from that model. He is, therefore, caught out because promotional activities which change consumers' tastes cannot be measured on a stable yardstick derived entirely from standard welfare analysis."¹¹ There are some non sequiturs in that argument, but I will deal with it in its own terms. Gould and Yamey have further claimed that I have not offered argument but only assertion on this point.¹² That charge I cannot accept.

In the first place, it is quite clear that Gould and Yamey have misunderstood the thrust of my argument and of the very paragraph they quote. I have viewed the reseller activities induced by r.p.m. as providing an economic good—information, entertainment, convenience, etc.—which is just as much an output of the economy as any other

10. Only in the special case in which the legislature determines both that r.p.m. usually restricts output and that the theory of second best leaves the effect of such restrictions utterly unknowable will the concept of consumer welfare become inoperative. But even here the concept of income distribution would decide nothing. R.p.m. creates larger incomes for the manufacturer and most resellers, and perhaps less income than would accrue in r.p.m.'s absence for some resellers. This fact seems to say nothing about r.p.m.'s desirability. The arguments in the text about the handling of overall income disparities seem applicable, and there seems no way to define such shifts in income as in themselves wrong. There are an infinite number of shifts due to commercial practices which we do not attempt to prohibit when consumer welfare is not thought to be involved. This special case seems open to solution only by reference to the presumption in favor of freedom of contract mentioned note 8 *supra*. But the outcome of this case does not, in any event, affect my argument which rests on the identification of r.p.m. as a means of creating efficiency.

11. Gould and Yamey, *Rejoinder*, 77 *YALE L.J.* 936, 938-39 (1968).

12. *Id.* 938.

product (or service).¹³ R.p.m., like vertical market division, is the means by which the manufacturer induces reseller provision of this product by making sure that the reseller can recover the product's cost. The process is closely analogous to the social recognition of property rights as a means of inducing economic activities. Contract law delegates to private persons the power to create property rights because of their superior knowledge of the efficiencies to be gained in particular situations. R.p.m. is best viewed as an instance of this general principle. The net effect of r.p.m. is to increase the amount of an existing product (or, more accurately, to enlarge the information component, for example, of a composite product consisting of a physical item and information about the item) which is offered to consumers. This analysis does not involve changes in consumer tastes any more than the offering of a greater amount of any existing product (or the change of any product's composition) changes tastes. The situation, therefore, is measurable by the "stable yardstick" Gould and Yamey require. If some consumers prefer to purchase the additional information, or other product, offered jointly with the physical item through r.p.m., the output of the economy has increased.

Gould and Yamey have not met this analysis, though the view of r.p.m. as changing the composition of products offered consumers appears not merely in the paragraph of my Reply they cite but in my prior pieces in this series.¹⁴ So far as I can tell, Gould and Yamey deal with the reseller activity induced by r.p.m. as though it did not count as an economic output but was instead merely something that changes tastes. I am not sure that this view of promotional activities is ultimately comprehensible, though it incorporates a common mode of speech. When a youth has classical music explained to him so that he comes to prefer Bach to the Beatles, have his tastes been changed or has the new information enabled him to relate classical music more effectively to existing tastes? It seems to me to depend upon whether "tastes" are defined as quite specific preferences or as basic psychologi-

13. I alluded to this view of promotional service as a product in my discussion of promotional activity as changing the composition of the product offered. It is an extract from this passage which Gould and Yamey quote and attack. Bork, *Reply*, 76 YALE L.J. 731, 733-34 (1967). Moreover, in Bork, *Part II*, 75 YALE L.J. 373 (1966), I repeatedly analyzed market division and price fixing as means of providing information and services, which should be recognized as economic outputs, and even referred to r.p.m. as a means of securing a uniform product which included sales effort as part of the product. *Id.* at 454-56. See generally Stigler, *The Economics of Information*, 69 J. POL. ECON. 213 (1961); Telser, *Supply and Demand for Advertising Messages*, 56 AMER. ECON. REV. PAPERS 457 (1966).

14. See note 13 *supra*.

cal traits. If the former, every new product or changed product has the effect of changing tastes and standard welfare analysis provides no rigorous way of judging it. If the latter, changes in taste infrequently, perhaps never, occur, and it is certainly unlikely that reseller promotion induced by r.p.m. is capable of changing such basic tastes. I am afraid that Gould and Yamey are operating with a concept, "changes in taste," that is so unrefined as to be practically useless in this discussion.

But I will assume, for the moment, that "changes in taste" refers to quite specific preference shifts and that the activity ("promotion") which induces such shifts is not in itself to be counted as an economic output. This pair of assumptions does indeed make it impossible rigorously to derive from the standard welfare model a conclusion that consumers are always better off after promotional activity has shifted their preferences. It is impossible to compare the value of two different outputs of the same economy which are responses to two different distributions of tastes. This observation, however, has little to do with appropriate public policy toward r.p.m. Two considerations indicate that the attempted consumer persuasion, which will sometimes succeed and sometimes fail, should be permitted to proceed.

I know of no ultimate standard by which it can be said that existing tastes are best and changes should be inhibited. We certainly do not make that assumption in the not-explicitly-economic sector of our lives. Nor does the fact that commercial persuasion is motivated by self-interest differentiate it from much, perhaps most, non-commercial persuasion. The appropriate rule (when we are dealing with products as to which consumer sovereignty is deemed desirable, *i.e.*, not addictive drugs and the like) would seem to be to leave sellers free to try to persuade and consumers free to respond or not. Whether or not consumers respond in a particular case, I know of no acceptable guide to consumer welfare other than the consumers' judgment of the matter.

There is a further point about the consistency of public policy that should be made. Apart from the merits of any of the arguments set out above, the fact is that we permit promotional activity in myriad forms in our society. If r.p.m. has as one of its major functions the more economical performance of that activity, I can see no rationality in singling it out for prohibition.

My answer to Gould and Yamey, then, is that I have analyzed the product or output made possible by r.p.m. in a way which makes it possible to state, on the basis of the standard welfare model, that consumers are better off. Should they reject that analysis, however, they

have not shown promotion to be harmful, only that nothing rigorous can be said of it in terms of the welfare model. I have shown, I believe, the reasons why, in that eventuality, public policy should be to permit r.p.m. The change-in-taste concept turns out to alter nothing.

E. *The Output Criterion*

Since Gould and Yamey understood that I was grounding my argument in welfare theory, and since that theory refers to the output of the economy as a whole, I am surprised that they managed also to believe that my output criterion related to the individual firm rather than to the economy as a whole. The misunderstanding is of no practical significance, however, for they and I have consistently argued the issues relevant to resource allocation in the total economy, *i.e.*, whether or not r.p.m. is likely to create restrictions of output.

To dispel any possible lingering confusion I will summarize the method by which a court should apply standard welfare assumptions. The judge should apply the concepts of price theory to the agreement, structure, or activity called into question in order to determine whether it is likely to create a restriction of output (create or increase a divergence between price and marginal cost). If not, the presumption is that the agreement or activity was motivated by the desire to achieve a more efficient utilization of resources. The judge may wish to go on, as I have in these articles, to understand how more efficient resource use is achieved, but in strict logic he need not. The presumption is that the creation of or increase in a divergence between price and marginal cost restricts the output of the industry and, more importantly, of the economy as a whole, while more efficient resource use increases both outputs. In some cases both effects may be present and the judge will have to estimate roughly the net effect. This is not our present case, however, for my argument is that the r.p.m. desired by a manufacturer not in collusion with other manufacturers has only the effect of creating efficient resource use. Inferences from price theory to welfare conclusions are proper and made necessary by the fact that the court has no feasible means of measuring directly the sizes of efficiencies, divergences between marginal costs and prices, or outputs.

The result of this sorting out of Gould and Yamey's suggested qualifications to standard welfare analysis is to perceive that when examined with any precision these qualifications evaporate as guides to public policy with respect to r.p.m. The standard welfare model which I outlined in the beginning of this piece appears to be entirely adequate to the task of judging r.p.m. The next question is whether,

within that model, the application of the concepts of price theory supports or weakens the case for r.p.m. I turn to that question now.

II. Price Theory

Professors Gould and Yamey have not undertaken to attack the entire case I made for r.p.m. but to pose certain objections which seem to them to outweigh the affirmative case. Since these objections do not seem valid, I will not attempt to estimate what would be the pros and cons of r.p.m. if they were valid. I will deal first with the attempted rehabilitation of the four Gould and Yamey counter-examples and then with other specific objections.

A. *The Four Counter-Examples*

The first Gould and Yamey counter-example consisted of an attempt to show that advertising differed from promotion induced through r.p.m. because advertising is asserted to be a fixed cost which does not affect output while r.p.m. increases marginal costs and does affect output. There was no limitation on this counter-example as originally put and I responded by pointing out that advertising would also be a marginal cost since any seller plans his advertising expenditures and output at one time, recognizing the interdependence of his decisions. Furthermore, the seller varies his expenditures and his output as experience teaches him their relationship more precisely.

It now appears, however, that Gould and Yamey are using a novel definition of fixed costs. Such costs are not identified by the fact that they cannot be varied in the relevant time period but by a state of mind gratuitously attributed to the entrepreneur. Advertising becomes, according to Gould and Yamey, a fixed cost simply because a hypothetical manufacturer insists upon so regarding it. This argument is not merely inconsistent with standard price theory, but is also divorced from reality and constitutes a device by which any and all marginal costs can be made fixed when that suits the debater's purposes.

We are asked to imagine a world in which a manufacturer is able to select the "best" advertising campaign without considering its relation to his sales and is inclined thereafter to take his level of advertising expenditure as a "given."¹⁵ One can only note that this man has a beautifully sequential mind, one which keeps in separate compartments decisions which crucially affect each other. In any world outside

15. Gould and Yamey, *Rejoinder*, 77 *YALE L.J.* 936, 939-40 (1968).

that of the hypothetical he would doubtless have to be accompanied by a guardian. Granted an equivalent freedom to postulate irrational economic behavior, I can show that advertising may be the *only* variable cost. My manufacturer decides first upon his "best" output and then regards that factor as "given." Henceforward, the only expenditure he will vary is his advertising. Thus, paralleling Gould and Yamey, we see that advertising is variable and wages, depreciation, raw materials, electricity, and so on and on, are all fixed costs and do not affect output. Postulating normal intelligence in the manufacturer, however, we would expect him to determine his advertising campaign, its effect upon his sales, and his proper output jointly. Advertising expenditure is then a marginal cost.¹⁶

It should be noted, moreover, that if we accepted Gould and Yamey's hypothetical as a possibly accurate version of reality, the result would be to show that, on this ground at least, r.p.m. is preferable to advertising. It is in the social interest that output should vary with real marginal costs. Gould and Yamey suggest that r.p.m. has that effect automatically but advertising may not because the manufacturer is free to disregard the impact of advertising on his sales. If that were significant, it would merely mean that advertising leaves the manufacturer free to misallocate resources by failing to regard it as what it is, a variable or marginal cost.

The first counter-example is either unrelated to reality or demonstrates the social superiority, in this respect, of r.p.m. to an advertising campaign.

The second and third counter-examples are sought to be rehabilitated by the curious maneuver of saying that my analysis of them rests upon an assumption of perfect ease of entry into all industries. This is simply not the case, as a reading of my prior response will show.¹⁷

The second counter-example purported to demonstrate that all the manufacturers in an industry might individually choose r.p.m. only to discover that they were all worse off for it. Without mentioning entry, I pointed out that the situation would not be stable because it would then be in the interests of some manufacturers and resellers to abandon r.p.m. This is true of the manufacturers and resellers already

16. Advertising can be made into a fixed cost, of course, by viewing it all as past advertising whose results were not as expected. Then the manufacturer would make new price and output decisions and would be unable to vary the past advertising expenditure, but that is certainly not significant. All past expenditures are fixed in this sense. Even past payments for promotional activities through r.p.m. are fixed costs.

17. Bork, *Reply*, 76 YALE L.J. 731, 734-36 (1967).

in the industry. If I had discussed entry, I might properly have pointed out that the situation envisaged by Gould and Yamey would have made entry more attractive, but I believe the counter-example to stand refuted without reference to entry.

The third counter-example was offered by Gould and Yamey to show that a monopolist manufacturer might use r.p.m. to slow the entry of large-scale resellers. My response did not posit any degree of ease or difficulty of entry but was and is that r.p.m. would not be an effective tool for the purpose specified since, whatever the entry conditions, r.p.m. would not make them more difficult but would either be neutral or make entry more attractive. The clarification of this point leaves the second and third counter-examples and my answers to them precisely where they were after the last exchange.

The fourth counter-example imagined the non-collusive use of r.p.m. by oligopolists to lessen the unsettling effects upon their non-competitive way of life of price competition at the reseller level. I pointed out that this tactic would introduce service and promotional competition which would lessen the benefits to be derived, that the practice had serious costs, and that the benefits to be derived were in any event less than would be attained through collusion. The non-collusive use of r.p.m. for this purpose, therefore, seems even less profitable than its use as a tool for policing actual collusion between manufacturers, a case which Gould and Yamey had agreed was unlikely.¹⁸

The whole counter-example is unrealistic in any event. If the oligopolists are able to work out techniques of this sort without collusion, and are then able to withstand continued reseller pressure for greater profit margins which would lead to pushing one product over the others, they hardly need the device of r.p.m. They can equally well, by parallel and non-collusive oligopolistic behavior, refuse to give price concessions to finance the competition at the retail level. I doubt very much that this tight formation flying without collusion is as common as some commentators suppose, but if it is, it should lead to solutions of the sort just mentioned rather than to elaborate schemes which cost more and accomplish less.

18. Gould and Yamey, *Professor Bork on Vertical Price Fixing*, 76 YALE L.J. 722, 725 n.10 (1967). I do not understand the distinction made in or the basis for their conditional withdrawal of that agreement in *Rejoinder*, 77 YALE L.J. 936, 942 (1968). It seems to me obvious that the non-collusive use of r.p.m. as a means of suppressing competition is less likely than its collusive use by a manufacturers' cartel. See Bork, *Reply*, 76 YALE L.J. 731, 737-38 (1967). I need not rehearse here the arguments indicating the improbability of even the collusive use of r.p.m. by manufacturers wishing to inhibit defection from a cartel. See Bork, *Part II*, 75 YALE L.J. 373, 411-15 (1966).

B. *The Side Effects of R.P.M.*

Gould and Yamey point out that the manufacturer using r.p.m. may have effects upon other goods sold by the same resellers and hence effects upon the resellers and upon consumers.¹⁹ Gould and Yamey discuss these side effects as if they were both inevitably detrimental and unique to r.p.m. In fact, they are neither.

The beneficial aspects of r.p.m. for resellers are apparent. When a manufacturer finds r.p.m. profitable, most of his resellers will also find it profitable as to his goods. This is a plus factor Gould and Yamey do not mention which will offset the detrimental side effects they posit. But there is no basis, in any event, for their supposition that the side effects themselves should usually be detrimental. They suppose it likely that resellers constrained by r.p.m. as to some products will be able to attract fewer customers to their stores and so will sell less of other products. On the contrary, if the r.p.m. succeeds by inducing successful promotional activity, as it must if the manufacturer is to find it worthwhile, more persons will be attracted to that store, and the reseller's prospects for selling other goods will be enhanced. This last remark is speculative but less so than the adverse possibilities imagined by Gould and Yamey. It is inconceivable that the manufacturer using r.p.m. should wish to weaken his outlets through the side effects of r.p.m., and certainly resellers who were injured would make their supplier aware of that fact.

Gould and Yamey's ruminations about the possible side effects of r.p.m. are idle, in any event, since almost all methods of distribution, as well as of production, have such effects. Both national advertising and reseller price cutting, for example, clearly have side effects upon resellers' sales of other products, and these effects may be either beneficial or harmful. Side effects occur when the manufacturer pays the salaries of salesmen for the promotion of his products in retail outlets, gives his resellers promotional materials, or contributes to reseller advertising of his products. No reason has been advanced why r.p.m.'s side effects are either usually harmful or different from any other

19. Gould and Yamey, *Rejoinder*, 77 YALE L.J. 936, 942-44 (1968). Some of the side effects imagined by Gould and Yamey seem impossible. They suppose, for example, that r.p.m. may be less beneficial than a manufacturer using it expects because "resellers [may] use the additional margin to cut prices of other goods or to provide services in respect of other goods." *Id.* 944 n.19. If it paid resellers to cut the prices of other goods, they would do so in any event. Additional income from price-maintained products is no more relevant to that decision than additional income from stock investments. Precisely the same analysis applies to the provision of promotional services with respect to other products.

distributive strategy. It is difficult to take this argument of Gould and Yamey seriously.

C. *Manufacturer Supervision of Reseller Activities*

I am at a loss to know why Gould and Yamey think it significant that r.p.m. involves control by one firm of one of the activities of another. So does every contract or working arrangement between two firms. It is a ubiquitous form of integration known as contract integration and has great economic advantages in many situations over ownership integration. Such control is often essential to the creation of efficiency.²⁰ The analogy between the use of r.p.m. and other normal management decisions, therefore, is not false but exact.

III. The Question of Standards of Proof

Professors Gould and Yamey and I have engaged in a discussion of the appropriate public policy toward r.p.m. Their latest piece raises the issue of the standard of proof to which discussants are to be held and I think it proper to close with a few words on that subject.

In my original piece, I attempted to demonstrate that there seems no reason to think r.p.m. would create restrictions of output but, on the contrary, there seem many reasons to think it enables the provision of an activity (read "service" or "product," if that seems preferable) that consumers are willing to pay for. I have argued the case in terms of the probabilities shown by the application of basic price theory. I do not contend that I have proved the case for r.p.m. in the sense that further analysis cannot possibly show me to be wrong. I do maintain that my arguments have not been answered by Professors Gould and Yamey. But Gould and Yamey seem to require something more of me; repeatedly they use language which seems to demand something approaching a mathematical demonstration that my case for r.p.m. holds in every imaginable circumstance. They insist, for example, that I prove the proposition: "R.p.m. always decreases (or else leaves unchanged) the divergence between price and marginal cost."²¹

I confess an inability to supply proof of the requisite mathematical and final nature. But the demand that I should is wholly unfair and unreasonable. I have offered an analysis based on conventional welfare

20. See R. Coase, *The Nature of the Firm*, in READINGS IN PRICE THEORY 331 (Stigler and Boulding eds. 1952).

21. Gould and Yamey, *Rejoinder*, 77 YALE L.J. 936, 946 (1968).

and price theory. Gould and Yamey have failed to shake that analysis in any respect. That should be enough. I do not suppose that anyone has demonstrated rigorously that plant investment, research and development, the hiring of salesmen, or any other hopefully profitable activity that businessmen undertake "always decreases (or else leaves unchanged) the divergence between price and marginal cost." It seems to me sufficient in such matters to show that there is no coherent theory which leads one to predict a restriction of output and that there is a coherent theory which predicts an efficient use of resources.

To require more than this is to create a presumption against every business activity until someone has rigorously demonstrated that never, under any circumstances, could that activity have an adverse impact. Policy discussion cannot intelligently be carried on under such rules. I would ask Professors Gould and Yamey to take to heart their own excellent dictum: "In advocating policy one must, of necessity, make do with what theoretical and empirical knowledge is available. We may bemoan our incomplete knowledge, but we shall wait forever if we wait on complete knowledge before tackling practical questions."²² Measured by that standard, I submit, the affirmative case for r.p.m. has been demonstrated.

22. *Id.* 945.

The Yale Law Journal

Volume 77, Number 5, April 1968

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Renewal*

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"Undesirables" from Public Housing*

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