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**BUSINESS ELECTRONICS CORP. V. SHARP
ELECTRONICS CORP.: MONSANTO'S PROGENY
AND THE CONGRESSIONAL PROPOSAL TO
CODIFY THE PER SE RULE AGAINST
VERTICAL PRICE FIXING**

Antitrust laws protect competition, not competitors.¹ Protection of vigorous price competition as a means of promoting consumer welfare² and economic efficiency has always been at the heart of this maxim. Section 1 of the Sherman Antitrust Act proscribes attempts to unreasonably interfere with the free-market forces that determine prices.³ In 1911, the United States Supreme Court first established that vertical price fixing was just such an unreasonable restraint of trade.⁴ Although Congress permitted a "fair trade" exemption to the Sherman Act for a time,⁵ in the ensuing seventy-eight years the Court reaffirmed the per se proscription against vertical price fixing in every case in which the issue arose.⁶ Recently, however, the executive and judicial branches of the Federal Government have challenged this absolute proscription against vertical price fixing as potentially creating market imperfections and discouraging efficient economic behavior.⁷

Theorists from the "Chicago School" of antitrust law propounded an

1. *Brown Shoe Co. v. United States*, 370 U.S. 294, 320 (1962).

2. Recognizing that the primary purpose of antitrust law is the promotion of consumer welfare, the United States Supreme Court has called the Sherman Antitrust Act a "consumer welfare prescription." *NCAA v. Board of Regents*, 468 U.S. 85, 107 (1984) (quoting *Reiter v. Sonotone Corp.*, 442 U.S. 330, 343 (1979)).

3. Sherman Antitrust Act of July 2, 1890, ch. 647, 26 Stat. 209 (current version at 15 U.S.C. §§ 1-7 (1982)). Section 1 prohibits "[e]very contract, combination . . . or conspiracy, in restraint of trade or commerce among the several States or with foreign nations." *Id.* § 1.

4. *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911). The Court did not actually use the phrase "illegal per se" in *Dr. Miles*. One of the first cases to hold that price fixing was illegal per se was *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 223 (1940).

5. See *infra* notes 85-89 and accompanying text.

6. See, e.g., *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 108 S. Ct. 1515 (1988); *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752 (1984); *Albrecht v. Herald Co.*, 390 U.S. 145 (1968); *White Motor Co. v. United States*, 372 U.S. 253 (1963); *United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960); *Schine Chain Theatres, Inc. v. United States*, 334 U.S. 110 (1948), *overruled on other grounds*, *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752 (1984); *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707 (1944); *Interstate Circuit, Inc. v. United States*, 306 U.S. 208 (1939); *United States v. A. Schrader's Son, Inc.*, 252 U.S. 85 (1920).

7. See *infra* text accompanying notes 101-49.

"efficiency" theory that urges the elimination of the per se rule because vertical price fixing may promote efficiency and competition.⁸ The Chicago School⁹ conflicts with traditional antitrust theory, which supports per se prohibitions against vertical price fixing and advocates the view that reasonable and vigorous price competition is more economically efficient and beneficial.¹⁰ The Chicago School's efficiency theory, however, has gained acceptance in modern legal circles¹¹ and has created a movement to overturn the precedent establishing vertical price fixing as illegal per se.

The efficiency theories of the Chicago School gained powerful proponents in the Reagan administration.¹² Despite empirical studies indicating the adverse economic effects of vertical price fixing,¹³ the Reagan administration

8. See generally Bork, *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division*, 75 YALE L.J. 373 (1966). Under this theory, increases in output promote efficiency and competition. *Id.* at 403-05. Price restraints imposed on a distributor by a manufacturer promote efficiency and competition because the manufacturer's goal is to increase output, not prices. *Id.* Manufacturers would not want to impose price restraints unless they were output enhancing. *Id.* Therefore, vertical price restraints are procompetitive and efficient. The manufacturer establishes a price or price level that induces a distributor to provide customer services, such as advertising, promotion, repair, and credit services, that the manufacturer has determined the customer wants, and that will persuade more customers to purchase the product. *Id.* at 429, 453-61. If the convenience that the customer realizes from these services more than offsets the utility the customer loses from the increase in the product's price, demand and output rise. If the utility from the services is less, the manufacturer adjusts the price and/or the level and quality of services to maintain output. *Id.* at 473; see also R. BORK, *THE ANTITRUST PARADOX* (1978); Baxter, *Vertical Restraints and Resale Price Maintenance: A 'Rule-of-Reason' Approach*, 14 ANTITRUST L. & ECON. REV. 13 (Issue 4, 1982); Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6 (1981).

9. This school is also sometimes called the "consumer welfare" school after the theories developed by former Judge Robert Bork in his book *The Antitrust Paradox*. See R. BORK, *supra* note 8. As one commentator has noted, this terminology is misleading because the effect of these policies may actually result in the transfer of wealth from the consumer to the retailers and manufacturers, leaving the consumer economically disadvantaged. See Gerla, *infra* note 98, at 3 n.10; see also H. HOVENKAMP, *ECONOMICS AND FEDERAL ANTITRUST LAW* § 2.3 (1985).

10. H. HOVENKAMP, *supra* note 9, at § 1.1. The traditional study of economics teaches that businesses unable to compete on a price basis succumb to more efficient rivals. *Id.* The consumer benefits from lower prices and higher quality products; the manufacturer realizes economies of scale and higher profits from increased output; and the economy benefits from a more efficient allocation of economic resources. *Id.* Section 1 of the Sherman Antitrust Act and antitrust laws in general are designed to protect against contracts, combinations, or conspiracies in restraint of trade formed for the purpose and with the effect of frustrating this result. See *Northern Pac. Ry. Co. v. United States*, 356 U.S. 1, 4-5 (1958).

11. See sources cited *supra* note 8.

12. See, e.g., ANTITRUST DIVISION, UNITED STATES DEPARTMENT OF JUSTICE, *VERTICAL RESTRAINTS GUIDELINES* (1985) [hereinafter GUIDELINES]; see also *infra* text accompanying notes 119-31.

13. See, e.g., S. REP. NO. 466, 94th Cong., 1st Sess. 3, *reprinted in* 1975 U.S. CODE CONG. & ADMIN. NEWS 1569, 1571-72 (citing a 1969 Economic Report of the President indicating

used the efficiency theory to defend its attempt to overturn the absolute prescription against this type of conduct.¹⁴ Two developments evidenced the administration's effort to eliminate or limit the application of the per se standard. First, the United States Department of Justice (DOJ) established a policy to intervene on behalf of defendants in private vertical price fixing actions.¹⁵ Second, the DOJ effectively abdicated responsibility for government enforcement of the vertical price fixing laws¹⁶ by ignoring or distinguishing the per se rule.¹⁷

The judiciary's view of vertical restraints also took on a decidedly Chicago School flavor. The Supreme Court's decision in *Continental T.V., Inc. v. GTE Sylvania, Inc.*,¹⁸ which applied the rule of reason to vertical nonprice restraints, evidenced the efficiency theory's impact on the legal treatment of vertical restraints.¹⁹ Seven years later, in *Monsanto Co. v. Spray-Rite Service Corp.*,²⁰ the Court relied on the efficiency rationale enunciated in *Sylvania*²¹

that the prices of goods were 18 to 27 percent higher under the fair trade laws and that consumers could save \$1.2 billion a year, \$2.1 billion adjusted for inflation, by eliminating the fair trade laws); Brief Amicus Curiae of Dayton Hudson Corp. for Petitioner at 14-17, *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752 (1984) (No. 82-914) (citing studies showing resale price maintenance's pernicious effect on prices, innovation and new businesses); see also *Retail Competition Enforcement Act, 1987: Hearings on S. 430, A Bill to Amend the Sherman Act Regarding Retail Competition, Before the Committee on the Judiciary, United States Senate, 100th Cong., 1st Sess. 105 (1987)* (statement of Mr. Monroe G. Milstein, President of the Burlington Coat Factory Warehouse Corp., citing a 1975 Justice Department study) [hereinafter *Hearings*]; *id.* at 69.

14. See, e.g., Brief for the United States as Amicus Curiae in Support of Petitioner, *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752 (1984) (No. 82-914) [hereinafter *Brief*]; GUIDELINES, *supra* note 12; see also *infra* notes 128-31 and accompanying text.

15. H.R. REP. NO. 421, 100th Cong., 1st Sess. 5 (1987).

16. S. REP. NO. 280, 100th Cong., 2nd Sess. 2 (1987). The existence of this policy is evidenced by the fact that the United States Department of Justice (DOJ) had not brought a single vertical price fixing action since 1981. *Id.*

17. *Id.* at 4-5.

18. 433 U.S. 36 (1977).

19. *Id.* at 58-59. In *Sylvania*, the Court overruled the per se standard for vertical nonprice restraints established ten years earlier in *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967). *Sylvania*, 433 U.S. at 58-59. The *Sylvania* Court established a presumption for application of the rule of reason standard, departure from which the Court held "must be based on demonstrable economic effect rather than . . . upon formalistic line drawing." *Id.* at 59. The Court's holding focused primarily on the "substantial scholarly and judicial authority supporting [the] economic utility" of vertical restraints. *Id.* at 57-58. Noting the potential procompetitive and efficiency-enhancing benefits of vertical restraints, the Court found that vertical restraints lack the pernicious effects on competition required of unreasonable restraints of trade. *Id.* at 54-58.

20. 465 U.S. 752 (1984).

21. *Sylvania*, 433 U.S. at 54-56. The Court also based its holding on the views advocated by the DOJ in an amicus brief filed on behalf of Monsanto. See *Brief, supra* note 14. The amicus brief advocated the elimination of the per se standard for vertical price fixing as inconsistent with the Court's decision in *Sylvania* and the requirement of proof of an explicit agree-

to narrow the breadth of the absolute prohibition against vertical price fixing by imposing a greater burden of proof on plaintiffs.²² This new evidentiary standard raised questions about the quantum of proof needed to prove a violation of the rule against vertical price fixing and consequently created confusion in the lower courts.²³ Four years later, *Business Electronics Corp. v. Sharp Electronics Corp.*²⁴ answered the question as to what quantum of evidence satisfied the *Monsanto* evidentiary standard.

Sharp Electronics Corporation (Sharp), a manufacturer of electronic products, granted Business Electronics Corporation (BEC), a discount retailer of electronic products, the sole Sharp dealership in the Houston area in 1968.²⁵ After disagreements between Sharp and BEC over sales quotas and discounting, Sharp granted a second dealership in the Houston area to Hartwell.²⁶ Upset about BEC's discounting and alleged "free riding"²⁷ practices, Hartwell approached BEC in an effort to convince BEC to end these practices and also complained to Sharp.²⁸ With no resolution forthcoming, Hartwell presented an ultimatum to Sharp in June 1973 threatening to end their relationship unless Sharp terminated BEC.²⁹ Sharp did so,³⁰ and BEC brought suit alleging that Sharp and Hartwell had conspired to terminate BEC in violation of section 1 of the Sherman Act.³¹

Sharp contended that it terminated BEC because of poor sales performance.³² BEC countered that its termination resulted from an agreement be-

ment on prices or price levels for application of the per se rule. *Id.* at 7-12, 19-29. The Court rejected the DOJ's suggestion to overturn the per se standard, but did adopt the more stringent standard of proof. *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 761 n.7, 764 (1984).

22. *Monsanto*, 465 U.S. at 764. In *Monsanto*, the plaintiff argued and the lower courts held that the termination of a dealer following or in response to a competing dealer's complaint about price cutting was illegal per se as a combination or conspiracy to fix prices. *Id.* at 757-59. The Court, however, refused to permit the inference of an agreement based on a termination following or in response to a competitor's complaints. Instead, the Court required the plaintiff to present evidence that excluded the possibility of independent action by the manufacturer. *Id.* at 764. The Court described the standard of evidence required to prove a conspiracy to fix prices as evidence that "tends to prove . . . 'a conscious commitment to a common scheme designed to achieve an unlawful objective.'" *Id.* (citing *Edward J. Sweeney & Sons, Inc. v. Texaco, Inc.*, 637 F.2d 105, 111 (3d Cir. 1980), *cert. denied*, 451 U.S. 911 (1981)).

23. S. REP. NO. 280, *supra* note 16, at 4.

24. 108 S. Ct. 1515 (1988).

25. *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 780 F.2d 1212, 1214-15 (5th Cir. 1986).

26. *Id.* at 1215.

27. *See infra* note 228.

28. 780 F.2d at 1215.

29. *Id.*

30. *Id.*

31. *Id.* at 1214.

32. *Id.* at 1215.

tween Sharp and Hartwell to eliminate price competition.³³ The case went to the jury with instructions that BEC's termination would violate section 1 of the Sherman Act if Sharp and Hartwell had agreed to terminate BEC because of its price cutting policy.³⁴ The jury found in favor of BEC.³⁵

On appeal, the United States Court of Appeals for the Fifth Circuit reversed and remanded.³⁶ The Fifth Circuit found error in the trial court's jury instruction that a finding of an agreement between Sharp and Hartwell to terminate BEC for its price cutting established a per se violation of the Sherman Act.³⁷ Holding that a manufacturer's termination of a dealer would be per se illegal only if effected pursuant to a price maintenance agreement with another dealer,³⁸ the court of appeals concluded that the evidence might be sufficient to find that Sharp terminated BEC pursuant to such a price agreement, and remanded the case for further proceedings consistent with its opinion.³⁹ However, in a short concurring opinion, one of the circuit judges invited the United States Supreme Court to address the confusing and uncertain area of vertical restraints.⁴⁰ When BEC appealed, the Supreme Court granted certiorari.⁴¹

The Supreme Court affirmed the Fifth Circuit's decision, holding that a vertical restraint of trade was not a per se violation under section 1 of the Sherman Act unless it included an agreement on prices or price levels.⁴² Writing for the majority, Justice Scalia reasoned that vertical restraints may promote economic efficiency and competition,⁴³ and concluded that economic analysis supported the view that the appropriate standard for non-price restraints was the rule of reason.⁴⁴ The Court again used the theoretical efficiencies and procompetitive benefits of vertical restraints to narrow the absolute prohibition against vertical price fixing.⁴⁵ The Court would not

33. *Id.* Evidence indicated that Hartwell usually complied with Sharp's suggested resale price list, and that both Hartwell and Sharp had attempted to obtain compliance with the price list from Business Electronics Corporation (BEC). *Id.* at 1219. In addition, BEC presented evidence that it was not "free riding," that its sales performance was equal to Hartwell's, and that BEC's termination was in response to Hartwell's complaints and ultimatum. *Id.*

34. *Id.* at 1215.

35. *Id.* at 1214.

36. *Id.* at 1220.

37. *Id.* at 1215.

38. *Id.* at 1218.

39. *Id.* at 1219-20.

40. *Id.* at 1221-22.

41. *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 482 U.S. 912 (1987).

42. *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 108 S. Ct. 1515, 1525 (1988). Justice Stevens and Justice White dissented. Justice Kennedy took no part in the decision.

43. *Id.* at 1519-20.

44. *Id.* at 1517, 1525.

45. *Id.* at 1519-20.

permit a jury to infer a vertical price fixing agreement merely from a dealer's termination following the complaints of a competing dealer.⁴⁶ Instead, the Court held that the plaintiff must present sufficient direct or circumstantial evidence to prove the existence of an explicit price agreement between the manufacturer and the complaining dealer.⁴⁷

Justice Stevens, writing in dissent, objected to the majority's mischaracterization of the restraint as a nonprice restraint.⁴⁸ He noted that the majority's decision attached more weight to the mere theoretical possibilities of economic and competitive benefits than to the real economic impact of this restraint on price competition.⁴⁹ Justice Stevens contended that such dealer terminations were more appropriately characterized as boycotts and, therefore, naked price-based restraints of trade in violation of the Sherman Antitrust Act.⁵⁰

Congress has reacted vigorously to the challenge to the per se rule and has taken various actions to prevent the erosion of the absolute prohibitions against vertical price fixing.⁵¹ Nevertheless, executive and judicial efforts to overturn or weaken the per se protections against vertical price fixing have succeeded.

This Note examines the development of antitrust law with respect to vertical restraints and the conflict between the judicial, executive, and legislative branches over the per se prohibition against vertical price fixing. It emphasizes the Supreme Court cases narrowing the per se standard applicable to vertical price restraints. Next, the Note focuses on the Justice Department's efforts to undermine private vertical price fixing actions and its failure to enforce the prohibitions against vertical price fixing under the Sherman Act. Against this background, the Note discusses the *Sharp* decision and its contribution to the gradual demise of the per se standard. The Note then critically analyzes the procompetitive and efficiency-enhancing benefits of vertical price fixing that the DOJ and the Supreme Court have advocated as a basis for narrowing or eliminating the per se standard. It then attempts to project the legal and economic impact of the *Sharp* decision. The Note reviews the actions that Congress is considering to turn back the assault on the per se standard. Finally, the Note concludes that Congress must codify the

46. *Id.* at 1520-21.

47. *Id.*

48. *Id.* at 1526 (Stevens, J., dissenting).

49. *Id.* at 1536.

50. *Id.* at 1531-32. Justice Stevens characterized the restraint as a horizontal restraint of trade; that is, a restraint of trade at the same level in the distribution system rather than a vertical restraint, which affects different levels in the distribution system. *Id.* at 1526; see *infra* note 54.

51. See *infra* text accompanying notes 156-72.

per se prohibition against vertical price fixing and restore the plaintiff's right to a jury trial where the plaintiff presents evidence sufficient to infer a price fixing conspiracy.

I. FUNDAMENTAL ISSUES IN THE VERTICAL RESTRAINTS CONTROVERSY

Every contract and every business relationship involves a restraint of trade.⁵² The Supreme Court has construed the Sherman Act, however, as proscribing only unreasonable restraints of trade.⁵³ Restraints of trade are classified as either horizontal⁵⁴ or vertical.⁵⁵ Vertical restraints, both price and nonprice, primarily affect intrabrand competition which is defined as competition among sellers of the same manufacturer's product.⁵⁶ Vertical price restraints, commonly known as resale price maintenance agreements,

52. Board of Trade of Chicago v. United States, 246 U.S. 231, 238 (1918).

53. *Id.* The Sherman Antitrust Act states that "(e)very contract, combination . . . is hereby declared to be illegal," and indeed, in early judicial interpretations of the Act, the proscription was literally construed to include what are today considered reasonable restraints. See *United States v. Trans-Missouri Freight Ass'n*, 166 U.S. 290 (1897), *overruled sub nom. Standard Oil Co. v. United States*, 221 U.S. 1 (1911). In *United States v. Trenton Pottery Co.*, 273 U.S. 392 (1927), the Court recognized the reasonableness standard for restraints of trade:

The essence of the law is injury to the public. It is not every restraint of competition and not every restraint of trade that works an injury to the public; it is only an *undue* and *unreasonable* restraint of trade that has such an effect and is deemed to be unlawful.

Id. at 395. (emphasis added).

54. ANTITRUST SECTION, AMERICAN BAR ASS'N, ANTITRUST LAW DEVELOPMENTS 28-55 (2d ed. 1984) [hereinafter DEVELOPMENTS]. A horizontal restraint is an agreement, either express or implied, among competitors of the same or similar product at the same level in the production-distribution system that affects the competitive relationship of the parties. *Id.* It may include, for example, an agreement as to prices, product, territories, or services. *Id.* Among the practices that have been deemed illegal per se are price fixing, *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940); cornering the market in a product, *id.* at 150; group boycotts, *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959); division of markets, *United States v. Topco Assoc., Inc.*, 405 U.S. 596 (1972); and fixing uniform customer discounts or credit terms, *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643 (1980). This Note will deal exclusively with vertical restraints.

55. H. HOVENKAMP, *supra* note 9, § 9.1. Vertical restraints are agreements between manufacturers and their dealers that restrict the freedom of dealers to market the product. *Id.* Typical vertical restrictions imposed on the dealer include resale price maintenance (vertical price fixing), location and customer restrictions, and exclusive dealing and tying arrangements. *Id.* §§ 8.1, 9.1; see also DEVELOPMENTS, *supra* note 54, at 55-108. Among the vertical practices that have been deemed to be illegal per se are vertical price fixing, *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911); and tying arrangements, *International Salt Co. v. United States*, 332 U.S. 392 (1947).

56. See *supra* note 55. In contrast, horizontal restraints affect interbrand competition: competition among the sellers of the same or similar product of different manufacturers. See *supra* note 54.

are agreements between manufacturers and dealers to fix the prices at which the dealer will resell the manufacturer's product.⁵⁷ Manufacturers impose vertical nonprice restraints to control the marketing and sale of the product.⁵⁸ Under current law, vertical restraints are subject to one of two standards: a *per se* rule or the rule of reason.

A *per se* rule of illegality is generally a conclusive presumption that a restraint is unreasonable.⁵⁹ Courts apply the standard to conduct deemed to have a "pernicious" effect on competition,⁶⁰ that is, conduct that "*almost always* results in adverse competitive effects, and *almost never* is justified by business reasons."⁶¹ The use of "almost" implies that the conduct may have procompetitive effects, but that collateral anticompetitive effects almost always outweigh these effects. The rationale for applying a *per se* rule is that it provides a "bright line" standard for the business and legal communities and results in administrative efficiency by deeming certain conduct illegal *per se* without proof of actual anticompetitive effects or injury.⁶²

A rule of reason standard, on the other hand, recognizes that certain restrictive conduct may promote economic efficiency or competition and attempts to balance these benefits against the potential anticompetitive effects of the conduct in order to determine whether the conduct is unreasonable.⁶³ The test, articulated by Justice Brandeis in *Board of Trade of Chicago v.*

57. 7 P. AREEDA, ANTITRUST LAW, ¶1437 (1986).

58. See *supra* note 55. Territorial and customer restrictions, exclusive dealership arrangements, and tying arrangements are the most common types of vertical nonprice restraints. *Id.*

59. *Arizona v. Maricopa County Medical Soc'y*, 457 U.S. 332, 344 (1982).

60. *Northern Pac. Ry. Co. v. United States*, 356 U.S. 1, 5 (1958). The Court defined those practices to which a *per se* standard should apply. The Court stated:

[T]here are certain agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use. This principle of *per se* unreasonableness not only makes the type of restraints which are proscribed by the Sherman Act more certain to the benefit of everyone concerned, but it also avoids the necessity for an incredibly complicated and prolonged economic investigation into the entire history of the industry involved, as well as related industries, in an effort to determine at large whether a particular restraint has been unreasonable—an inquiry so often wholly fruitless when undertaken.

Id.; see also *United States v. Container Corp. of America*, 393 U.S. 333, 341 (1969) (Marshall, J., dissenting) (defining the rationale of the *per se* standard).

61. Pitofsky, *The Sylvania Case: Antitrust Analysis of Non-Price Vertical Restrictions*, 78 COLUM. L. REV. 1, 12 (1978).

62. See *Maricopa County*, 457 U.S. at 343-44. Antitrust litigation is extremely complex, expensive, and time-consuming. *Id.* Judicial and business efficiencies are realized by avoiding the long, complex, and expensive trials required in rule of reason actions. *Id.* Thus, when a *per se* rule is applied, the judicial system and the business environment benefit from a relatively clear and concise statement of the conduct proscribed by the Sherman Act. *Id.*

63. *Board of Trade of Chicago v. United States*, 246 U.S. 231, 238 (1918).

United States,⁶⁴ requires a determination of whether the restraint merely regulates and thereby promotes competition, or whether it suppresses or destroys competition.⁶⁵ The typical rule of reason case requires a complex and time-consuming examination of the specific conduct, the product and geographic markets, the adverse and beneficial impact of this conduct on those markets, and the motives and justifications for the conduct.⁶⁶ Restraints that are not illegal per se are subjected to the rule of reason standard. A rule of reason action can be an extremely expensive process and is often difficult for a plaintiff to win. A per se standard avoids this costly fact-finding process because it requires proof only of the existence of the conduct.

II. DEVELOPMENT OF VERTICAL RESTRAINTS LAW

A. Vertical Price Restraints and the Sherman Act

In 1911, the Supreme Court established the illegality of vertical price fixing in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*⁶⁷ Dr. Miles, a manufacturer of proprietary medicines, required each wholesale and retail seller of its products to enter into a consignment or agency contract that fixed the prices at which the dealer could resell Dr. Miles' products.⁶⁸ Dr. Miles alleged that the defendant, a wholesaler, had obtained the company's products from Dr. Miles' agents and had sold them at less than the contractually set minimum prices.⁶⁹ Noting that agreements having no other purpose than to restrain competition and fix prices were injurious to the public,⁷⁰ the Court held the plaintiff's consignment contract invalid both at common law and under the Sherman Act.⁷¹

64. 246 U.S. 231 (1918).

65. *Id.* at 238. Justice Brandeis described the test as follows:

The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts.

Id.; see also *National Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679, 687-92 (1978) (providing a history and explanation of the rule of reason standard).

66. See Pitofsky, *supra* note 61, at 13.

67. 220 U.S. 373 (1911).

68. *Id.* at 394.

69. *Id.* at 382.

70. *Id.* at 408.

71. *Id.* at 409. Later decisions established that an explicit agreement was not required. An agreement may be inferred from a course of dealing, conduct, or other circumstances, or by acquiescence. See *United States v. Parke, Davis and Co.*, 362 U.S. 29, 43-44 (1960); *United*

Recognizing that the Sherman Act did not take away the manufacturer's right to choose with whom it would conduct business, the Court soon narrowed the scope of the *Dr. Miles* decision. In *United States v. Colgate & Co.*,⁷² the Court literally construed the Sherman Act's prohibition against contracts and combinations in restraint of trade. Colgate published a price list and urged dealers to conform to these prices.⁷³ In addition, Colgate announced that it would refuse to deal with any wholesalers or retailers that would not agree to maintain these prices.⁷⁴

Interpreting the proscriptions of the Sherman Act as reaching only contracts or combinations in restraint of trade, the Court held that a unilateral refusal to deal did not violate the Sherman Act.⁷⁵ The Court stated that, in the absence of an attempt to create a monopoly, the Sherman Act did not restrict the manufacturer's right to choose the parties with whom it would deal.⁷⁶ In addition, the manufacturer could announce in advance its pricing policy and those circumstances under which it would refuse to deal.⁷⁷

Although the *Colgate* principle recognized the manufacturer's right to unilaterally refuse to deal with a customer, the Court soon limited this principle. Three years later, in *FTC v. Beech-Nut Packing Co.*,⁷⁸ the manufacturer not only promulgated its pricing policy and announced its intention to refuse to deal with noncomplying dealers, but also established a system to enforce these pricing policies.⁷⁹ Beech-Nut solicited assurances from its dealers that they would maintain a certain price level and used these dealers to police other dealers in order to ensure compliance with its pricing policies.⁸⁰ Dealers violating Beech-Nut's pricing policies or selling to noncomplying dealers were terminated and boycotted.⁸¹ Beech-Nut would reinstate terminated dealers if they provided assurances of future compliance with Beech-Nut's pricing policies.⁸²

The Court concluded that these methods went beyond the manufacturer's

States v. Bausch & Lomb Optical Co., 321 U.S. 707, 723 (1944); *FTC v. Beech-Nut Packing Co.*, 257 U.S. 441, 455 (1922); *Frey & Son, Inc. v. Cudahy Packing Co.*, 256 U.S. 208, 210 (1921); *United States v. A. Schrader's Son, Inc.*, 252 U.S. 85, 99-100 (1920). *But see* *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 108 S. Ct. 1515, 1525 (1988).

72. 250 U.S. 300 (1919).

73. *Id.* at 303.

74. *Id.*

75. *Id.* at 307.

76. *Id.*

77. *Id.*

78. 257 U.S. 441 (1922).

79. *Id.* at 444-45.

80. *Id.* at 445-46.

81. *Id.*

82. *Id.* at 446.

right to refuse to deal enunciated in *Colgate*.⁸³ The Court held that Beech-Nut's enforcement system and the required dealer assurances of cooperation constituted a restraint of competition and unfair trade practice in violation of section 5 of the Federal Trade Commission Act.⁸⁴

While the courts generally continued to enforce the per se rule against vertical price fixing in the period after *Beech-Nut*, state pressure on Congress to permit a "fair trade" exemption from the Sherman Act⁸⁵ and a growing number of judicial decisions upholding state fair trade laws⁸⁶ prompted Congress to grant a fair trade exemption in 1937.⁸⁷ Growing discontent with the economic consequences of the state fair trade exemption⁸⁸ caused Congress

83. *Id.* at 454.

84. *Id.* at 444, 455. Under the Federal Trade Commission Act, ch. 311, § 5, 38 Stat. 717 (1914) (codified as amended at 15 U.S.C. § 45(a) (1982 & Supp. V 1987)), the FTC is empowered to condemn and suppress unfair methods of competition in commerce. By judicial interpretation, this includes enforcement of the Sherman Act. *Beech-Nut*, 257 U.S. at 453-55.

85. See E. KINTNER, 2 FEDERAL ANTITRUST LAWS § 10.16 (1980). In 1937, the year of passage of the federal fair trade exemption, 37 states had enacted fair trade laws and six other states had proposed them. See also *infra* notes 87-88.

86. See *Old Dearborn Distrib. Co. v. Seagram-Distillers Corp.*, 299 U.S. 183 (1936) (upholding the constitutionality of Illinois' Fair Trade Act); *Pep Boys, Manny, Moe & Jack, Inc. v. Pyroil Sales Co.*, 299 U.S. 198 (1936) (upholding the constitutionality of California's Fair Trade Act). State fair trade laws permitted manufacturers to control resale prices through vertical price fixing. Fair trade laws in California and Illinois were upheld by the Supreme Court in 1936. *Id.* at 201; *Old Dearborn*, 299 U.S. at 191-98.

87. Miller-Tydings Act of 1937, ch. 690, tit. VIII, 50 Stat. 693, *repealed by* Consumer Goods Pricing Act of 1975, Pub. L. No. 94-145, 89 Stat. 801. The Miller-Tydings Act exempted businesses in states authorizing resale price maintenance from the proscriptions of the Sherman Act. *Id.* In states without an authorizing statute, vertical price fixing was still held to be illegal per se. *Id.*

88. *Id.* Vertical price fixing in all contexts remained illegal per se until Congress passed the Miller-Tydings Act in 1937, amending the Sherman Act. *Id.* The Miller-Tydings Act permitted manufacturers to prescribe minimum prices for the intrastate resale of products bearing the "trademark, brand or name of the producer or distributor of such commodity" if such practice was lawful under state statute, common law or public policy. *Id.* The McGuire Act of 1952 expanded the power of the manufacturer to set minimum prices by binding non-parties to the resale price maintenance (RPM) contracts or agreements. Act of July 14, 1952, ch. 745, 66 Stat. 631, 632, *repealed by* Consumer Goods Pricing Act of 1975, Pub. L. No. 94-145, 89 Stat. 801. Thus, if one dealer in a state had entered into an RPM agreement with a manufacturer, then all other dealers in that manufacturer's product in the state were required to abide by the minimum prices. *Id.*

Both of these acts required "free and open competition with commodities of the same general class" in order for the manufacturer to be eligible for the exemption from the Sherman Act. Ch. 690, 50 Stat. at 693. The free and open competition requirement, however, in no way assured the consumer the benefits of vigorous price competition. One study, conducted by the Justice Department under President Nixon and cited in a 1969 Economic Report of the President, found that these fair trade practices increased the price of products by 18 to 27 percent. S. REP. NO. 280, *supra* note 16, at 2. Another study determined that if these acts were repealed, consumers would save approximately \$1.2 billion. *Id.* For these and other reasons, the number of states permitting resale price maintenance declined from a peak of 46 to 12 in 1975.

to rescind the exemption in 1975.⁸⁹

Following the enactment of the fair trade exemption, the Court continued its assault on the *Colgate* principle by further limiting the types of actions that the Court deemed unilateral. In *United States v. Bausch & Lomb Optical Co.*⁹⁰ and *United States v. Parke, Davis & Co.*,⁹¹ the Court reiterated its position on manufacturers' actions designed to enforce resale price systems. At issue in both cases was a system of prices and price enforcement similar to Beech-Nut's system.

As in *Beech-Nut*, the Court in *Bausch & Lomb* and *Parke, Davis* stressed the coercive and conspiratorial nature of the pricing system. The pricing policies in dispute went beyond mere unilateral refusals to deal or dealer acquiescence to the pricing systems.⁹² In each case, the Court found that the distributor and licensed dealers conspired to fix resale prices and limit sales, and held that the cooperative enforcement of the price system and boycotts of noncomplying dealers constituted a combination in restraint of trade in violation of the Sherman Act.⁹³

While affirming the *Colgate* principle of unilateral action in *Beech-Nut*, *Bausch & Lomb*, and *Parke, Davis*, the Court substantially limited *Colgate's* application, thereby restricting a manufacturer's ability to police and enforce

Recognizing the dampening effect that resale price maintenance had on price competition, Congress repealed the fair trade acts by passage of the Consumer Goods Pricing Act in 1975. Act of Dec. 12, 1975, Pub. L. No. 94-145, 89 Stat. 801 (*amending* 15 U.S.C. §§ 1, 45(a) (1982)). The Consumer Goods Pricing Act restored per se illegality to vertical price fixing without exception.

89. Consumer Goods Pricing Act of Dec. 12, 1975, Pub. L. No. 94-145, 89 Stat. 801 (*amending* 15 U.S.C. §§ 1, 45(a) (1982)). A number of reasons were cited for rescinding the fair trade exemption including its inflationary impact, a higher number of business failures, its facilitation of horizontal price fixing, and unnecessary advertising and sales services expenditures. *Hearings, supra* note 13, at 69-70. *See supra* note 88.

90. 321 U.S. 707 (1944). Bausch & Lomb's sole distributor, Soft-Lite, had a dual licensing system. *Id.* at 714-17. Wholesalers were licensed to sell pink-tinted eyeglass lenses at a fixed price to licensed retailers, and retailers were licensed to sell the lenses at locally prevailing prices to the public. *Id.* Pursuant to the licensing agreements, dealers were prohibited from selling to unlicensed or noncomplying dealers. *Id.* at 714. The system was enforced through surveillance of the licensed dealers and a lens identification system used to trace lenses sold to unlicensed dealers. *Id.* Dealers violating the license agreements were terminated. *Id.* at 715-16.

91. 362 U.S. 29 (1960). Parke, Davis had a pricing system that included minimum resale pricing and an enforcement program. *Id.* at 32-33. It issued a list of minimum resale prices and refused to sell to wholesalers who did not comply with the pricing scheme or who sold Parke, Davis products to non-complying retailers. *Id.* Parke, Davis enforced its resale pricing system with the cooperation of dealers and by threats of termination and boycotts of noncomplying retailers. *Id.* at 33-34. Noncomplying dealers were reinstated if they agreed to comply with Parke, Davis' pricing system. *Id.* at 35-36.

92. *Bausch & Lomb*, 321 U.S. at 723; *Parke, Davis*, 362 U.S. at 44.

93. *Bausch & Lomb*, 321 U.S. at 723; *Parke, Davis*, 362 U.S. at 45.

a system of suggested retail prices. Because such a system of enforcement requires cooperation and concerted action between the parties in the distribution system, the arrangement implies an agreement or combination that a court might, and in these cases did, find a restraint of trade.

After *Parke, Davis*, the Court had effectively limited the application of the *Colgate* principle to cases falling within the narrow *Colgate* fact pattern.⁹⁴ That is, a manufacturer could establish a price list, announce its policies with respect to terminating noncomplying dealers, and unilaterally refuse to deal with distributors that did not comply with its prices.⁹⁵ However, the manufacturer could not solicit assurances of compliance from dealers, enforce or coerce compliance from price cutters by enlisting the cooperation of other dealers to report them, or boycott price cutters in order to obtain compliance and then reinstate them.⁹⁶ This view survived until the modern Court reviewed *Colgate* in the context of a dealer-initiated termination in *Monsanto v. Spray-Rite Corp.*⁹⁷ By this time, the Reagan administration's appointments to the Court and growing acceptance of the Chicago School's efficiency theory provided the administration with the opportunity to effectively challenge the status of vertical restraints law.

B. *The Modern Trend: Vertical Restraints Promote Efficiency and Competition*

The economic efficiency theories of the Chicago School of antitrust law have significantly influenced the modern debate over the treatment of vertical price restraints.⁹⁸ These theories shaped the Reagan administration's

94. See, e.g., *George W. Warner & Co. v. Black & Decker Mfg. Co.*, 277 F.2d 787 (2d Cir. 1960). The Supreme Court's substantial narrowing of the *Colgate* principle prompted the *Black & Decker* court to comment that with respect to the status of *Colgate*, the Supreme Court "has left a narrow channel through which a manufacturer may pass even though the facts would have to be of such Doric simplicity as to be somewhat rare in this day of complex business enterprise." *Id.* at 790.

95. *Id.*

96. *Id.*

97. 465 U.S. 752 (1984).

98. See, e.g., Gerla, *Discounters and the Antitrust Laws: Faces Sometimes Should Make Cases*, 12 J. CORP. L. 1 (1986) (arguing that, contrary to efficiency theory position, discounters, the group primarily protected by the proscriptions against vertical price fixing, are economically efficient and enhance competition and consumer welfare); Scherer, *The Economics of Vertical Restraints*, 52 ANTITRUST L.J. 687 (1983) (disputing the economic theory of the Chicago School regarding vertical restraints); Comanor, *Vertical Price-Fixing, Vertical Market Restrictions, and the New Antitrust Policy*, 98 HARV. L. REV. 983 (1985) (questioning the vertical restraints analysis of the Chicago School, particularly Judge Bork's analysis); Pitofsky, *supra* note 61 (disputing many of the "efficiencies" supported by the efficiency theorists as a rationale for eliminating the proscription against vertical price fixing and cited by the *Sylvania* Court as a basis for overturning *Schwinn*); Pitofsky, *In Defense of Discounters: The No-Frills*

policy, which advocates legalization of vertical price restraints,⁹⁹ and placed the administration in opposition to Congress.¹⁰⁰ The parties have taken the conflict to the judiciary, and recent Supreme Court decisions indicate that the Chicago School's efficiency theory has gained adherents on the Court.

I. Pre-Reagan Judicial Treatment of Vertical Restraints

Although prior decisions demonstrated the Court's growing awareness and interest in the economic impact of their decisions, *Continental T.V., Inc. v. GTE Sylvania, Inc.*¹⁰¹ clearly evidenced the influence of Chicago School theories on the Court's treatment of vertical restraints. A vertical nonprice restraint, which the Court had only a decade earlier declared illegal per se in *United States v. Arnold, Schwinn & Co.*,¹⁰² triggered the *Sylvania* litigation. The Court reassessed and overruled *Schwinn*.¹⁰³ The Court rationalized its application of the rule of reason standard to vertical nonprice restraints on the basis of the potential efficiencies and procompetitive benefits of these restraints.¹⁰⁴ Intentionally or not, this decision set the stage for a challenge to the per se rule against vertical price fixing.

Sylvania, a television manufacturer, had terminated its wholesale dealers and developed a nonexclusive franchise system that limited the number of franchises in an area.¹⁰⁵ The system also required franchisees to sell the

Case for a Per Se Rule Against Vertical Price Fixing, 71 GEO. L.J. 1487 (1983) (disputing the efficiency theorists' arguments in support of eliminating the per se proscription against vertical price fixing).

99. Compare, e.g., GUIDELINES, *supra* note 12 and Brief, *supra* note 14 with R. BORK, *supra* note 8 and Posner, *supra* note 8.

100. Compare, e.g., GUIDELINES, *supra* note 12 and Brief, *supra* note 14 with H.R. REP. NO. 421, *supra* note 15 and S. REP. NO. 280, *supra* note 16.

101. 433 U.S. 36 (1977).

102. 388 U.S. 365 (1967). The history of the Court's treatment of vertical nonprice restraints illustrates the difficulty the Court has experienced in dealing with the economics of antitrust issues. In *White Motor Co. v. United States*, 372 U.S. 253 (1963), the Court applied the rule of reason standard to vertical nonprice restraints. Noting that not enough was known about the impact of these vertical arrangements on competition, the *White Motor* Court reversed a lower court decision applying the per se standard to nonprice restraints. 372 U.S. at 263-64.

Just four years later, however, the Court determined that it knew enough about the competitive effects of vertical restraints and overruled the *White Motor* decision in *Schwinn*. In *Schwinn*, the Court held the defendant's vertical customer and location restrictions illegal per se. 388 U.S. at 382. In dicta, the Court indicated that vertical nonprice restraints imposed on dealers constituted restraints on alienation by manufacturers that could so unreasonably restrict competition that a violation of the Sherman Act would result. *Id.* at 380.

103. *Sylvania*, 433 U.S. at 58.

104. *Id.* at 54-56.

105. *Id.* at 38.

merchandise only from prescribed locations.¹⁰⁶ A disagreement arose between Continental, a successful franchisee, and Sylvania over the location of a new franchise near a Continental location.¹⁰⁷ In protest of Sylvania's action, Continental opened an outlet at another location without Sylvania's approval.¹⁰⁸ Sylvania terminated Continental for violating the franchise agreement, and Continental challenged the franchise contract's location restraint as a violation of the Sherman Act.¹⁰⁹

The trial court, following *Schwinn*, found Sylvania in per se violation of the Sherman Act.¹¹⁰ The Court of Appeals for the Ninth Circuit reversed the decision on the grounds that the jury instruction, which required a finding of a per se violation, was erroneous.¹¹¹ The Supreme Court affirmed the Ninth Circuit's decision.¹¹²

Reasoning that vertical nonprice restraints may promote economic efficiency and competition, the Court held that petitioners failed to show that such restraints had a "pernicious effect on competition or that they lack[ed] any redeeming virtue."¹¹³ Noting that the vertical nonprice restraints in *Sylvania* actually stimulated interbrand competition,¹¹⁴ the Court overruled *Schwinn* and held that the rule of reason was the appropriate evidentiary standard to apply to vertical nonprice restraints.¹¹⁵ Although the Court reaffirmed its support of the per se rule against vertical price fixing,¹¹⁶ Justice White noted in a prescient concurring opinion that these same procompetitive and efficiency justifications could support the application of the rule of reason standard to all vertical restraints¹¹⁷ and, therefore, the Court's opinion called into question the absolute prohibition against vertical price fixing.¹¹⁸

106. *Id.*

107. *Id.* at 39.

108. *Id.*

109. *Id.* at 40.

110. *Id.* at 41.

111. *Id.*; see also *GTE Sylvania, Inc. v. Continental T.V., Inc.*, 537 F.2d 980, 982, 987-88 (9th Cir. 1976), *aff'd*, 433 U.S. 36 (1977).

112. *Sylvania*, 433 U.S. at 59.

113. *Id.* at 58 (quoting *Northern Pac. Ry. v. United States*, 356 U.S. 1, 5 (1958)).

114. *Id.* at 38-39.

115. *Id.* at 57-59.

116. *Id.* at 51 n.18.

117. *Id.* at 70 (White, J., concurring).

118. *Id.* According to Justice White in his concurring opinion, the Court did not satisfactorily distinguish between price and nonprice restraints in its *Sylvania* decision. *Id.* at 69-70. The majority disposed of the issue by stating that the per se illegality of vertical price restraints involved significantly different issues of analysis and policy. *Id.* at 70. Justice White noted that the Court's failure to adequately explain why vertical price fixing did not give rise to the same efficiencies called into question the per se rule against vertical price fixing. *Id.*

2. Vertical Price Fixing Developments Under the Reagan Justice Department

During the Reagan terms, the administration pursued a policy designed to restrict the scope of and, ultimately, eliminate the per se rule against vertical price restraints. Under the direction of the Department of Justice, the Reagan administration policy succeeded in undermining both public and private vertical price fixing actions under the Sherman Act.¹¹⁹ First, the administration abdicated its responsibilities with respect to enforcement of the per se prohibition against vertical price fixing. Despite the number of private vertical price fixing suits brought during the Reagan administration,¹²⁰ the DOJ had not instituted one government vertical price fixing action through 1986.¹²¹

Second, through a series of writings¹²² and amicus filings,¹²³ the DOJ attempted to undermine private vertical price fixing actions and urged the Supreme Court to overturn the per se rule against vertical price fixing. Under an "amicus intervention program" established in 1981,¹²⁴ the DOJ intervened on behalf of defendant manufacturers in private vertical price fixing antitrust suits.¹²⁵ One of the DOJ's most controversial briefs was filed in 1983 with the Supreme Court in *Monsanto Co. v. Spray-Rite Service Corp.*¹²⁶ Therein, the DOJ urged the Court either to overturn the per se prohibition against vertical price fixing or to apply the per se standard only to explicit agreements to fix prices or price levels.¹²⁷

Finally, the DOJ promulgated a set of "Vertical Restraints Guidelines"¹²⁸ that detailed the DOJ's policy with respect to enforcement of vertical re-

119. H.R. REP. NO. 421, *supra* note 15, at 2.

120. In the period from the *Monsanto* decision to 1987 alone, approximately 70 private vertical price fixing actions were instituted. *Id.*

121. S. REP. NO. 280, *supra* note 16, at 2. In addition, the DOJ opened only six investigations during the Reagan administration, compared to the 40 it opened in the period 1976 to 1981. *Id.* at 23.

122. *See, e.g., infra* text accompanying notes 128-31.

123. *See, e.g., infra* text accompanying notes 124-27.

124. H.R. REP. NO. 421, *supra* note 15, at 5.

125. *Id.*

126. 465 U.S. 752 (1984); *see* Brief, *supra* note 14; *see also* Brief for the United States as Amicus Curiae, *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752 (1984) (No. 82-914) (urging the Supreme Court to grant Monsanto's petition for writ of certiorari). The amicus filing in *Monsanto* was controversial for three reasons: (1) Congress fully supported the per se standard for vertical price fixing, (2) the status of the per se standard was not an issue that either party raised in the action, and (3) *Monsanto* was an important and very visible case, and therefore, there was no assurance that the Court would not address the per se issue. *See* H.R. REP. NO. 421, *supra* note 15, at 4-10; S. REP. NO. 280, *supra* note 16, at 3-5.

127. Brief, *supra* note 14, at 13-29.

128. GUIDELINES, *supra* note 12.

straints law.¹²⁹ Purporting to deal only with vertical nonprice restraints, the guidelines essentially established a no-action policy with respect to vertical price restraints.¹³⁰ The guidelines stated that where a manufacturer had a bona fide distribution program embodying nonprice and price restraints, the DOJ would analyze the system using the rule of reason under either of two conditions. The DOJ would use the rule of reason if there was no "direct or circumstantial evidence (other than effects on price) establishing an *explicit* agreement as to specific prices," or where "the nonprice restraints [were] *plausibly* designed to create efficiencies . . . and the price restraint [was] merely ancillary to the nonprice restraint."¹³¹

3. *Judicial Treatment of Vertical Price Restraints During the Reagan Administration*

*Monsanto Co. v. Spray-Rite Service Corp.*¹³² was the first major vertical price fixing case of the Reagan era. The Supreme Court's decision in *Monsanto* can be seen as a victory for the Reagan administration's efforts to undermine or eliminate the per se rule against vertical price fixing. In *Monsanto*, the DOJ submitted an amicus brief urging the Court to overturn the per se rule.¹³³ While the Court declined to address the issue directly,¹³⁴ it placed an additional burden of proof on the plaintiff not found in other areas of antitrust law, thereby significantly narrowing the per se standard's scope as applied to vertical price fixing.¹³⁵

The issue in *Monsanto* was whether a manufacturer's unilateral action¹³⁶ or the concerted action of the manufacturer and a complaining dealer caused a dealer's termination. Spray-Rite, a distributor of Monsanto products, sued

129. *Id.* The DOJ's enforcement policy was based on the potential procompetitive effects of vertical restraints commonly cited in Chicago School literature, including realization of economies of scale from a reduction in the number of outlets and lower distribution costs, increased provision of sales services, discouragement of free-riding by discounters, *see infra* note 228, improved product quality and safety, reduced transaction costs, and facilitation of new producer entry into the market. *Id.* at 14-15.

130. H.R. REP. NO. 421, *supra* note 15, at 6-7.

131. *See* GUIDELINES, *supra* note 12, at 10-11 (emphasis added).

132. 465 U.S. 752 (1984).

133. *See* Brief, *supra* note 14.

134. *Monsanto*, 465 U.S. at 761 n.7.

135. *Id.* at 764. A congressional report commented: "Not only must a plaintiff seeking to reach the jury *prove* a conspiracy, but he also must *disprove* the existence of any or all hypothetical explanations for the manufacturer's conduct that 'might justify a dealer termination.' To many observers, such a test appears to be unnecessary and unfairly harsh." H.R. REP. NO. 421, *supra* note 15, at 14.

136. Unilateral or independent actions of a manufacturer in refusing to deal with or terminating a dealer are legitimate actions not within the scope of the Sherman Act. *United States v. Colgate & Co.*, 250 U.S. 300 (1919); *see supra* notes 72-77 and accompanying text.

Monsanto under section 1 of the Sherman Act for terminating Spray-Rite's distributorship.¹³⁷ Spray-Rite alleged that competing distributors' complaints about Spray-Rite's failure to comply with Monsanto's suggested prices resulted in its termination.¹³⁸ Further, Spray-Rite alleged that Monsanto and the complaining distributors conspired to fix resale prices and took other actions in furtherance of that conspiracy.¹³⁹ Monsanto countered that Spray-Rite was terminated because of its failure to provide adequate nonprice promotional services.¹⁴⁰

The jury found that Monsanto's actions were in furtherance of a conspiracy to fix resale prices and, therefore, were a per se violation of section 1 of the Sherman Act.¹⁴¹ The United States Court of Appeals for the Seventh Circuit affirmed the district court's decision and established a standard of proof under which a dealer's termination following the complaints of a rival dealer could give rise to an inference of concerted action.¹⁴²

The Supreme Court affirmed the district court's decision but reversed the appeals court's standard of proof and established a more stringent standard.¹⁴³ Reasoning that allowing a jury to infer an agreement to fix prices from a dealer's termination following the complaints of a rival dealer might deter economically efficient and procompetitive conduct,¹⁴⁴ the Court declared that mere evidence of dealer complaints was not sufficient to prove an agreement to fix prices.¹⁴⁵ Rather, the plaintiff must present direct or circumstantial evidence that tends to exclude the possibility of independent action by the manufacturer and distributor.¹⁴⁶ The Court, however, found that the plaintiff had met this more stringent burden of proof and affirmed the lower court decision.¹⁴⁷

Monsanto defined a new evidentiary standard for proof of a vertical conspiracy to fix prices. The Court shifted the burden of proof to the plaintiff to disprove independent action and, thus effectively revitalized *Colgate's* dis-

137. *Monsanto*, 465 U.S. at 757.

138. *Id.* at 758-59.

139. *Id.* at 757-58. Actions in furtherance of the conspiracy included boycotting Spray-Rite and the use of compensation programs, areas of primary responsibility and shipping policies to fix, maintain, or stabilize prices. *Id.*

140. *Id.* at 757.

141. *Id.* at 757-58.

142. *Id.* at 758-59.

143. *Id.* at 759.

144. *Id.* at 762-64.

145. *Id.* at 764.

146. *Id.* The Court stated that the plaintiff's evidence must reasonably tend to prove that the manufacturer and others had "a conscious commitment to a common scheme designed to achieve an unlawful objective." *Id.*

147. *Id.* at 765, 768.

inction between concerted and independent action.¹⁴⁸ Again, the Court based its holding on the efficiencies resulting from conduct that might be perceived as price fixing.¹⁴⁹ The decision was controversial and confusing for a number of reasons.

First, many lower courts interpreted the decision as requiring direct or circumstantial evidence of an explicit agreement between the manufacturer and complaining dealer to fix prices or price levels.¹⁵⁰ Second, Congress and the lower courts interpreted *Monsanto* as removing from the jury its traditional antitrust charge of drawing inferences of a conspiracy from a set of facts.¹⁵¹ In some cases, the lower courts required the plaintiff to prove that an explicit agreement existed rather than allowing the jury to infer an agreement from a termination "following" or "in response to" complaints from a dealer.¹⁵² Third, the Court's decision revealed an unjustifiable lack of confidence in the jury's ability to distinguish legitimate from illegitimate business practices.¹⁵³ Fourth, by requiring evidence disproving independent action on the part of the manufacturer and dealer, the *Monsanto* decision substantially increased the quantum of proof needed for a plaintiff's action to reach

148. *Id.* at 762-63; see also *supra* text accompanying notes 72-77.

149. *Monsanto*, 465 U.S. at 762-64.

150. See *Garment Dist., Inc. v. Belk Stores Serv., Inc.*, 799 F.2d 905 (4th Cir. 1986) (manufacturer's action in terminating a discounter was unilateral, despite evidence of the coercive acts of a rival dealer and a pretextual nonprice restraint's defense), *cert. denied*, 108 S. Ct. 1728 (1988); *McCabe's Furniture, Inc., v. La-Z-Boy Chair Co.*, 798 F.2d 323 (8th Cir. 1986) (application of per se standard to a dealer termination was in error because nonprice as well as price factors motivated the termination), *cert. denied*, 108 S. Ct. 1728 (1988); *Morrison v. Murray Biscuit Co.*, 797 F.2d 1430 (7th Cir. 1986) (wholesale dealer failed to prove he was terminated pursuant to a conspiracy to suppress price competition between a supplier and a rival dealer); *Westman Comm'n Co. v. Hobart Int'l, Inc.*, 796 F.2d 1216 (10th Cir. 1986) (in the absence of evidence of an agreement to raise prices, an agreement between a supplier and dealer to terminate a rival dealer is not illegal per se), *cert. denied*, 108 S. Ct. 1728 (1988); *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 780 F.2d 1212 (5th Cir. 1986) (district court erred in finding manufacturer's termination of a dealer a per se violation of the Sherman Act without proof of an explicit agreement on prices), *aff'd*, 108 S. Ct. 1515 (1988). Although the *Monsanto* decision did not specifically state that an explicit agreement was required, many jurisdictions have interpreted it that way. The evidence presented in the above cases was sufficient to prove a conspiracy between a manufacturer and dealer to terminate a rival dealer for price cutting, but the appeals courts generally held that *Monsanto* did not permit an inference of a conspiracy to suppress price competition. H.R. REP. NO. 421, *supra* note 15, at 21-25. Something more than evidence of complaints was needed. *Id.* Exoneration of the manufacturers was invariably based on the procompetitive benefits of nonprice restraints. *Id.*

151. H.R. REP. NO. 421, *supra* note 15, at 17-18.

152. See cases cited *supra* note 150.

153. H.R. REP. NO. 421, *supra* note 15, at 19-20. This is a function that the jury freely exercises in other areas of antitrust, such as monopolization cases under section 2 of the Sherman Act. *Id.*

the jury.¹⁵⁴ Finally, the decision impliedly attached greater weight to the potential efficiencies and procompetitive benefits of the conduct than to the very real impact of the dealer's termination on price competition.¹⁵⁵

4. Congressional Response: Vertical Price Fixing is Illegal Per Se

Congress expressed its unequivocal support of the per se rule against vertical price fixing when it passed the Consumer Goods Pricing Act of 1975,¹⁵⁶ which rescinded the state fair trade exemption. The subsequent executive actions and judicial decisions undermining the rule¹⁵⁷ understandably troubled Congress and prompted legislative action to prevent further erosion of the rule. First, Congress used its funding powers to restrain the DOJ's efforts to undermine the per se rule.¹⁵⁸ Prior to the DOJ's oral argument of its *Monsanto* amicus filing, Congress passed the DOJ appropriation bill for 1984.¹⁵⁹ The bill prohibited the DOJ from using its funds to urge the reversal of the per se rule against vertical price fixing.¹⁶⁰

Second, Congress passed a resolution vehemently rejecting the DOJ's non-enforcement policy with respect to vertical restraints law.¹⁶¹ The DOJ's lack of enforcement of vertical restraints law during the Reagan administra-

154. *Id.* at 16-17; see *infra* text accompanying notes 207-08.

155. See *supra* text accompanying notes 207-73. The *Monsanto* Court noted that a finding of a per se violation might deter legitimate manufacturer-dealer communication designed to assure that the product reaches the consumer efficiently. *Monsanto*, 465 U.S. at 763-64. Dealer terminations "in response to" complaints from a dealer about price cutting have a very real, although indirect, impact on prices and are equivalent to a boycott. See Gerla, *supra* note 98, at 9-12.

156. Pub. L. No. 94-145, 89 Stat. 801 (1975) (amending 15 U.S.C. §§ 1, 45(a) (1982)); see *supra* note 89; text accompanying notes 85-89; see also H.R. REP. NO. 421, *supra* note 15, at 8.

157. See *supra* text accompanying notes 119-55.

158. Departments of Commerce, Justice, and State, the Judiciary and Related Agencies Appropriations Act, 1984, Pub. L. No. 98-166, § 510, 97 Stat. 1071, 1102-03 (1983) [hereinafter 1984 Appropriations Act]. The congressional funding restrictions directed that no funds could be used for any activity the purpose of which was to overturn or alter the per se prohibition against resale price maintenance in effect under the federal antitrust laws. *Id.* Additional funding restrictions were passed in 1986, Department of Justice Appropriation Act, 1986, Pub. L. No. 99-180, § 605, 99 Stat. 1141, 1169-70 (1985) [hereinafter 1986 Appropriations Act]; 1987, Department of Justice Appropriation Act, 1987, Pub. L. No. 99-500, § 605, 100 Stat. 1783-45, 1783-73 (1986); and 1988, Department of Justice Appropriation Act of 1988, Pub. L. No. 100-202, § 605, 101 Stat. 1329-8, 1329-38 (1987), all of which prohibited the DOJ from using funds for any activity designed to alter the per se prohibition against vertical price fixing.

159. 1984 Appropriations Act, *supra* note 158.

160. *Id.* The bill, in effect, prevented Assistant Attorney General William Baxter from orally arguing the DOJ's *Monsanto* amicus brief, which urged the reversal of the per se rule, before the Supreme Court. *Id.*; see also H.R. REP. NO. 421, *supra* note 15, at 5.

161. 1986 Appropriations Act, *supra* note 158, at 1169-70. The DOJ had not brought a single government price fixing case since 1981 and had conducted only six investigations, none of which were ever brought to trial. S. REP. NO. 280, *supra* note 16, at 2, 23.

tion greatly concerned Congress.¹⁶² Four months after the expiration of the 1984 funding restriction,¹⁶³ the DOJ released the "Vertical Restraints Guidelines of January 23, 1985," which established its policy on enforcement of vertical restraints law.¹⁶⁴ Congress viewed the guidelines as another attempt to influence judicial treatment of vertical price fixing and to dilute the per se standard by blurring the distinction between price and nonprice restraints.¹⁶⁵ In response, Congress passed the Vertical Restraints Guidelines Resolution.¹⁶⁶ In the resolution, Congress rejected the DOJ's enforcement policy and interpretation of the law as stated in the guidelines and demanded that the Attorney General recall the guidelines.¹⁶⁷ In addition, Congress stated in the resolution that the courts should not construe the guidelines as an accurate representation of either current antitrust law or Congress' position on vertical price fixing.¹⁶⁸

Finally, the *Monsanto* decision itself prompted a congressional reaction. Congress saw the *Monsanto* decision as hindering private antitrust actions and remedies at a time when government enforcement of vertical price fixing law was lacking.¹⁶⁹ Although the *Monsanto* decision reaffirmed the per se standard for vertical price fixing, it was the first evidence that the Reagan administration's "efficiency" view was beginning to influence lower court and Supreme Court decisions relating to vertical price fixing. In response, Congress proposed amendments to the Sherman Act that would restore the per se standard to its pre-*Monsanto* status.¹⁷⁰ These bills, pending when the

162. S. REP. 280, *supra* note 16, at 2, 23.

163. Upon assurances from the DOJ that it would enforce vertical price fixing law as interpreted by the Supreme Court, the 1984 funding restriction against the DOJ's vertical price fixing activities was allowed to expire on October 1, 1984. Thus, the 1985 bill deleted all references to vertical restraints. *Id.* at 3.

164. See GUIDELINES, *supra* note 12; text accompanying notes 128-31.

165. 1986 Appropriations Act, *supra* note 158, at 1169.

166. *Id.* at 1169-70.

167. *Id.*

168. *Id.* The Resolution stated that the DOJ's Vertical Restraints Guidelines:

- (1) are not an accurate expression of the Federal antitrust laws or of congressional intent with regard to the application of such laws . . . ;
- (2) shall not be accorded any force of law or be treated by the courts of the United States as binding or persuasive; and
- (3) should be recalled by the Attorney General.

Id.

169. H.R. REP. NO. 421, *supra* note 15, at 2.

170. S. 430, 100th Cong., 1st Sess., 133 CONG. REC. S1483-84 (daily ed. Feb. 2, 1987); H.R. 585, 100th Cong., 1st Sess., 133 CONG. REC. H254 (daily ed. Jan. 8, 1987). These proposals sought to amend the Sherman Act in order to codify the per se standard against vertical price fixing and establish the quantum of evidence sufficient to meet the plaintiff's burden under the per se standard. S. REP. NO. 280, *supra* note 16, at 9-12; H.R. REP. NO. 421, *supra* note 15, at 30-31. Both proposals eliminate *Monsanto's* requirement of presenting evidence

100th Congress ended, were reintroduced in the 101st Congress.¹⁷¹

Congress' rescission of the state fair trade exemption in 1975 reestablished its position on vertical price fixing and the per se standard. The *Monsanto* decision prompted congressional action which reaffirmed Congress' unequivocal and consistent support for the per se rule against vertical price fixing and evidenced Congress' intent to maintain the standard. This clear record of congressional support for the per se standard existed prior to the time the Court heard *Business Electronics Corp. v. Sharp Electronics Corp.*¹⁷² Consequently, *Sharp* provided an opportunity for the Court either to defer to Congressional intent by reinstating the pre-*Monsanto* standard, or to adopt the administration's position by further limiting or overturning the per se standard.

III. *BUSINESS ELECTRONICS CORP. V. SHARP ELECTRONICS CORP.*

In *Sharp*, the Court further narrowed the absolute prohibition against vertical price fixing in the context of a dealer termination. Justice Scalia, writing for the majority, addressed the issue of the standard applicable to a dealer termination and affirmed the appeals court's application of the rule of reason.¹⁷³ Characterizing the restraint at issue as a vertical nonprice restraint, Justice Scalia stated that the Court's holdings in *Sylvania* and *Monsanto* dictated a presumption for applying the rule of reason to vertical nonprice restraints.¹⁷⁴ Justice Scalia found no evidence that an agreement to terminate a discounting dealer, without an additional agreement between the manufacturer and a complaining dealer on prices, restricted competition or

that tends to exclude independent action and instead allow the jury to infer an illegal agreement from a dealer's termination in response to or because of complaints from a rival dealer. S. REP. NO. 280, *supra* note 16, at 11; H.R. REP. NO. 421, *supra* note 15, at 31-32.

171. The new Senate and House versions of these bills were introduced in the first session of the 101st Congress. The Senate version, S. 865, was introduced on April 19, 1989, 135 CONG. REC. 4435, 4437 (daily ed. Apr. 19, 1989). The House version, H.R. 1236, was introduced on March 2, 1989. 135 CONG. REC. H510, 527 (daily ed. Mar. 2, 1989). The major change from the previous versions is the prohibition of the conduct permitted by the Court in *Sharp*. In response to the Supreme Court decision in *Sharp*, the new versions proscribe agreements between a seller and a dealer to terminate another dealer for its pricing policies, whether or not prices or price levels are agreed upon. *Id.*

172. 108 S. Ct. 1515 (1988).

173. *Id.* at 1517, 1525.

174. *Id.* at 1520. Citing *Sylvania* and *Monsanto*, Justice Scalia stated that departure from the rule of reason standard should "be based on demonstrable economic effect rather than . . . upon formalistic line drawing." *Id.* (citing *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 58-59 (1977)). Noting that vertical nonprice restraints have certain procompetitive benefits, Justice Scalia declared that vertical nonprice restraints had not been shown to have such a "pernicious effect on competition and lack of any redeeming virtue" as to warrant a standard of per se illegality. *Id.* at 1519 (citing *Sylvania*, 433 U.S. at 58).

reduced output.¹⁷⁵ To the contrary, Justice Scalia indicated that such restraints could promote competition and economic efficiencies¹⁷⁶ that would not be realized if the Court applied a per se standard.

Justice Scalia then focused on the interbrand-intrabrand competition distinction. Noting that interbrand competition is the principal concern of antitrust law,¹⁷⁷ Justice Scalia declared that as long as the per se standard protected interbrand competition, it was not needed to protect intrabrand competition.¹⁷⁸ First, Justice Scalia stated that interbrand competition provided a significant check on attempts to exploit intrabrand market power.¹⁷⁹ Second, a per se standard of illegality encompassing all vertical restraints created a perverse incentive for manufacturers to vertically integrate, which would result in fewer small businesses and higher market concentration.¹⁸⁰ Third, vertical nonprice restraints, unlike vertical price restraints, do not facilitate cartelization¹⁸¹ and, therefore, do not require a per se standard to

175. *Id.* at 1521.

176. *Id.* at 1519-20. Manufacturers can use these restraints 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. . . . [and to] induce retailers to engage in promotional activities or to provide service and repair facilities necessary to the efficient marketing of their products. . . . The availability and quality of such services affect a manufacturer's goodwill and the competitiveness of his product. Because of market imperfections such as the so-called 'free-rider' effect, these services might not be provided by retailers in a purely competitive situation

Id. (quoting *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 55 (1977)).

177. *Id.* at 1519.

178. *Id.* at 1520.

179. *Id.* Theoretically, if a manufacturer attempts to exploit intrabrand market power by raising prices, consumers will switch to the lower priced product of a rival manufacturer. *Sylvania*, 433 U.S. at 52 n.19. This result, however, depends on the convenience to consumers, the amount of competition, and the ability of consumers to exploit this competition. *Id.* at 54.

180. *Sharp*, 108 S. Ct. at 1520. This argument assumes that if the per se standard prevents the utilization of nonprice restraints to achieve distributive efficiencies, the manufacturer will vertically integrate by purchasing or establishing retail businesses, thereby eliminating the small, independent distributorships. *Sylvania*, 433 U.S. at 57 n.26. A manufacturer's decision to vertically integrate, however, involves more than just a consideration of distributive efficiencies. Although transaction costs may decline, a manufacturer must also consider the capital investment and expertise required and the additional risk inherent in a decision to vertically integrate. See Halverson, *An Overview of Legal and Economic Issues and the Relevance of the Vertical Merger Guidelines*, 52 ANTITRUST L.J. 49, 80-81 (1983). Therefore, the decision is not simply a choice between vertical nonprice restraints or vertical integration.

181. *Sharp*, 108 S. Ct. at 1520. A cartel is a combination or association of companies joined together to control competition in the pricing, marketing, or production of a product. A cartel often attempts to monopolize a particular product or industry. The critical issue with respect to vertical price fixing by members of a cartel is whether a group of manufacturers is able to stabilize or maintain prices at an agreed level. Manufacturers often use competitors' retail prices to monitor compliance with the agreed prices. See Pitofsky, *supra* note 61, at 16.

prevent anticompetitive conduct.¹⁸²

Next, Justice Scalia reasoned that the application of the per se standard to manufacturers' actions that are not based on price agreements would deter or penalize legitimate communication or conduct between manufacturers and dealers.¹⁸³ One of the rationales for the *Sylvania* Court's rejection of the per se standard for vertical nonprice restraints, he noted, was to allow such procompetitive communication or conduct.¹⁸⁴ Justice Scalia reasoned that imposing a per se standard in this situation would encourage terminated discounters to allege price fixing in order to attack terminations for nonprice reasons and would deter legitimate and competitively useful conduct.¹⁸⁵ The rule of reason adequately protected dealers against unreasonable restraints of trade. Rejecting the plaintiff's¹⁸⁶ and the dissent's¹⁸⁷ remaining arguments, Justice Scalia concluded that economic analysis supports the view that vertical restraints should not be illegal per se unless they include an explicit agreement to fix prices.¹⁸⁸

In a lengthy dissent, Justice Stevens rejected the majority's characterization of the issue as one concerning vertical nonprice restraints.¹⁸⁹ Justice Stevens contended that an agreement initiated by a complaining dealer to terminate a competing dealer because of the competing dealer's price cutting policies was not a nonprice restraint, but rather an unreasonable restraint on price competition.¹⁹⁰ A more proper analysis of the issue, he stated, would have focused on horizontal restraints and the distinction between naked and

182. *Sharp*, 108 S. Ct. at 1520. The dissent argued and this Note argues that a termination of a dealer for price cutting is a price restraint and, therefore, will facilitate cartelization. *Id.* at 1530 (Stevens, J., dissenting).

183. *Id.* at 1520 (majority opinion).

184. *Id.*

185. *Id.* at 1521.

186. *Id.* at 1524-25. Justice Scalia rejected BEC's arguments that the application of the per se standard to this vertical restraint was controlled by precedent on horizontal restraints and by vertical restraint cases that established that no explicit agreement on prices or price levels was required to apply the per se standard. *Id.* He also disagreed that a price agreement will always follow from a dealer's termination and noted that a dealer's termination may quite plausibly be motivated by a desire to induce dealer services rather than to fix prices. *Id.* at 1523.

187. *Id.* at 1522-23. Justice Scalia rejected the dissent's characterization of BEC's termination as a naked restraint of competition at the retail level. *Id.* He stated that there is a quite plausible purpose of this restraint; specifically, to induce a dealer to provide services, which therefore makes the restraint ancillary. *Id.* In addition, Justice Scalia concluded that BEC's termination was not a horizontal restraint because a manufacturer imposed it, not other dealers. *Id.*

188. *Id.* at 1525.

189. *Id.* at 1526 (Stevens, J., dissenting).

190. *Id.*

ancillary restraints of trade.¹⁹¹ The dissent asserted that BEC's termination was comparable to a group boycott, therefore, the Court's holding in *United States v. General Motors Corp.*¹⁹² should control.¹⁹³

Justice Stevens noted that past Court decisions had permitted reasonable covenants in restraint of trade if they were ancillary to the main purpose of a contract and did not violate the rule of reason.¹⁹⁴ Justice Stevens argued, however, that the subject restraint was neither a term of nor ancillary to Sharp's dealership agreements with BEC and Hartwell and was, therefore, not a vertical nonprice restraint.¹⁹⁵ He found the majority's reliance on *Sylvania* misplaced. Distinguishing *Sylvania's* contractual location restraint, Justice Stevens noted that Sharp had not imposed any vertical nonprice restraints, such as location, territory, or customer requirements, on either BEC or Hartwell.¹⁹⁶ Because neither BEC nor Hartwell were contractually obligated to provide dealer services, the procompetitive benefits that the majority posited as resulting from this "nonprice restraint" were mere possibilities.¹⁹⁷ Thus, BEC's termination was a naked restraint with no purpose but to suppress price competition.¹⁹⁸

Justice Stevens next examined the character of the termination in order to illustrate its anticompetitive nature. He contended that the Court should have focused on the character of the agreement and its economic consequences, rather than on the number of parties involved in the agreement.¹⁹⁹ Criticizing the majority's summary disposal of *General Motors* and *Klor's, Inc. v. Broadway-Hale Stores, Inc.*,²⁰⁰ Justice Stevens found that the principal elements of a group boycott established in those cases were also present here.²⁰¹ He argued that BEC's termination accomplished the same purpose,

191. *Id.*

192. 384 U.S. 127 (1966) (concerted action by automotive dealers, automotive dealer associations, and the automobile manufacturer to terminate business dealings and refuse to do business with discounters was an unlawful conspiracy or group boycott in restraint of trade).

193. *Sharp*, 108 S. Ct. at 1531-32.

194. *Sharp*, 108 S. Ct. at 1526-27. Justice Stevens noted, for example, that contractual covenants not to compete in a particular business, when reasonable, are permitted in contracts for the sale of a business. *Id.* The main purpose of the ancillary restraint must be to protect one party from the unrestrained competition of another. *Id.* But where it serves only to restrain trade and destroy competition, it is unreasonable. *Id.*

195. *Id.* at 1528.

196. *Id.*

197. *Id.*

198. *Id.* at 1529.

199. *Id.* at 1530-32.

200. 359 U.S. 207 (1959) (concerted action among retailers, manufacturers, and distributors of appliances to terminate business dealings and refuse to deal with plaintiff retailer was a group boycott or conspiracy in restraint of trade).

201. *Sharp*, 108 S. Ct. at 1532. Recounting the typical elements of a group boycott, Justice

and differed only in degree from that struck down in *General Motors*.²⁰² The agreement, Justice Stevens concluded, was a naked horizontal restraint on price competition rather than an ancillary vertical nonprice restraint designed to further the manufacturer's distributional policies.²⁰³

Finally, Justice Stevens criticized the majority's interpretation of *Sylvania* as permitting the elimination of intrabrand competition based only on the "quite plausible" assumption of improvements in interbrand competition.²⁰⁴ He asserted that *Sylvania* required something more than a mere possibility of a benefit to interbrand competition. Justice Stevens concluded that this restraint provided no demonstrable improvements to interbrand competition, therefore, the restraint should not evade the Court's rule of per se illegality by the mere possibility of procompetitive benefits.²⁰⁵ He criticized the majority's "plausible purposes" justification for this naked restraint as contrary to one of the fundamental objectives of the Sherman Act — to foster price competition.²⁰⁶

IV. VERTICAL RESTRAINTS: AN ECONOMIC CONTROVERSY AND AN EVIDENTIARY DEBATE

Underlying the Court's decision in *Sharp* is a growing dissatisfaction with the per se rule against vertical price fixing. While the *Sharp* Court preserved the per se standard in form, it significantly narrowed its applicability to cases where an aggrieved party can prove the existence of an explicit agreement on prices or price levels, thereby undermining the standard's vitality.²⁰⁷ After *Monsanto* and *Sharp*, the terminated dealer's burden of proof increased substantially; indeed, it has been equated to a burden requiring proof of a formal offer and acceptance.²⁰⁸ In establishing such a stringent evidentiary stan-

Stevens noted that BEC's termination was not an independent action controlled by the *Colgate* decision, but a concerted action motivated by an ultimatum from a complaining dealer. *Id.* at 1529-32. Elimination of price competition on the dealer level, rather than the violation of a vertical nonprice restraint, was the primary motivating factor in the termination of BEC. *Id.* at 1532. The economic consequences arising from the coercive activities of one competing dealer on the manufacturer are as pernicious as those resulting from the coercive activities of a number of competing dealers. *Id.* Thus, the sole difference between this action and a group boycott was the number of parties involved. *Id.*

202. *Id.* at 1531-32.

203. *Id.* at 1532.

204. *Id.* at 1536. If a per se standard could be avoided simply by positing a "plausible purpose," then the same purposes could be cited to evade the application of a per se standard in other price fixing cases where it might be argued that the defendant could provide better services. *Id.*

205. *Id.*

206. *Id.*

207. *Id.* at 1525.

208. See H.R. REP. NO. 421, *supra* note 15, at 16-17.

dard, the Court has effectively enabled a manufacturer and dealer to circumvent the per se standard and fix or maintain prices by terminating a discounting dealer. The complexity and expense of a rule of reason case will deter terminated dealers from bringing actions against manufacturers and will likely allow manufacturers to terminate dealers abusively and with impunity.

The increase in the plaintiff's burden of proof will result in less legal protection for discounters and more dealer terminations. The loss of discounters will result in a number of unfavorable economic consequences. First, inflationary pressures²⁰⁹ and higher prices²¹⁰ will follow the reduction in price competition. Second, reduced consumer choice will result in lower consumer utility.²¹¹ Third, inefficient manufacturers and dealers will insulate themselves from the competitive market through vertical price fixing.²¹² Finally, business failures will increase and new business start-ups will decrease in a vertical price fixing environment.²¹³ *Monsanto* and *Sharp* reduce both intrabrand and interbrand competition and, thus, create less competitive industries, diminish consumer welfare, and produce less flexible and efficient price and distribution systems.

However, the Court and the administration argue that less price competition is beneficial if it results in better sales services, eliminates market imperfections such as free riding, and increases output by attracting new dealers to

209. See *Hearings, supra* note 13, at 69.

210. A 1987 study conducted in one city for the Senate Judiciary Committee found that consumers pay 18 to 30 percent less in discount stores than in full-price retail stores. See *Hearings, supra* note 13, at 1 (opening statement of Sen. Metzenbaum, Acting Chairman, citing a staff study). Studies conducted just prior to the passage of the Consumer Goods Pricing Act of 1975 confirm this statistic. S. REP. NO. 280, *supra* note 16, at 2.

211. See, e.g., Gerla, *supra* note 98, at 3-5. All consumers do not desire the same level of prices and services, and the elimination of the discounter will result in more standardized and uniform distribution channels. Discounters provide the customer with alternative price/product/service mixes that increase consumer choice and maximize consumer welfare. *Id.*

212. Pitofsky, *supra* note 61, at 15-16. At the manufacturer level, inefficient manufacturers will be able to maintain prices at levels that reduce dealer pressure to lower wholesale prices, thereby insulating themselves from the competitive markets. *Id.* Neither the manufacturer nor dealer will have to compete on the merits of the product or on a price basis. Promotional or nonprice competition will take over as it has done in the automobile industry. The reduction in price pressure on the manufacturer from the discounter will result in less competitive industries. See generally Gerla, *Competition on the Merits — A Sound Industrial Policy for Antitrust Law*, 36 U. FLA. L. REV. 553 (1984).

213. S. REP. NO. 466, *supra* note 13, at 3, reprinted in 1975 U.S. CODE CONG. & ADMIN. NEWS 1569, 1571-12. New dealers are generally more efficient than established dealers and compete primarily on a price basis. *Hearings, supra* note 13, at 105 (statement of Mr. Monroe G. Milstein, Chairman of Burlington Coat Factory, citing 1975 Justice Department Study). *Id.* at 102. Vertical price fixing will deter the establishment of new businesses if these businesses cannot compete on a price basis. *Id.*

invest in the capital and labor required to distribute more efficiently.²¹⁴ The *Sharp* Court termed these factors the "quite plausible purpose[s]" of Sharp's termination of BEC.²¹⁵ Those advocating the elimination of the per se rule against vertical price fixing also utilize these same arguments.²¹⁶

The Chicago School and the DOJ argue that economic efficiency factors should control in determining an evidentiary standard for vertical restraints.²¹⁷ They contend that the procompetitive benefits and efficiencies of vertical restraints justify at least applying the rule of reason to vertical restraints if not a standard of per se legality.²¹⁸ Traditional antitrust advocates oppose the elimination of the per se standard and argue that vertical price fixing promotes neither efficiency nor consumer welfare.²¹⁹ Although procompetitive benefits and efficiencies may result from vertical price fixing, advocates contend that the pernicious effects on competition outweigh such speculative benefits.

The legal debate over the appropriate standard to apply to vertical restraints, specifically price restraints, understandably arises from the inability of scholars to agree on the effects of these restraints on the business environment. Economics scholars agree, and empirical evidence shows, that prices are higher under vertically-fixed prices than under unrestrained price competition.²²⁰ Scholars disagree, however, over whether the procompetitive benefits realized from vertical price fixing sufficiently warrant the suppression of price competition.²²¹ The *Sharp* Court decided that the benefits to competition and efficiency, which a dealer termination might produce, so outweighed the effects on price competition that the plaintiff's additional evidentiary burden of proving an agreement on price or price levels was justified.

214. *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 108 S. Ct. 1515, 1519-20 (1988). Under this theory, the demand induced by increased services and information more than offsets the dampening effect of higher prices on demand. See *supra* note 8. The argument implies that higher prices result in more or better services. There is no empirical evidence to show, however, that one follows directly from the other.

215. *Sharp*, 108 S. Ct. at 1522.

216. See, e.g., Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 ANTITRUST L.J. 135 (1984); Posner, *supra* note 8; Abbott, *Paradox Regained: Towards a New Economic Approach to Vertical Restraints Policy*, 48 GEO. WASH. L. REV. 565 (1980); Bork, *supra* note 8; Telser, *Why Should Manufacturers Want Fair Trade?*, 3 J.L. & ECON. 86 (1960).

217. See *supra* note 8.

218. See, e.g., sources cited *supra* note 8; GUIDELINES, *supra* note 12; Brief, *supra* note 14.

219. See, e.g., *supra* note 10; Scherer, *supra* note 98; Gerla, *supra* note 98.

220. S. REP. NO. 280, *supra* note 16, at 2.

221. Compare, e.g., Scherer, *supra* note 98 and Pitofsky, *supra* note 98 with Posner, *supra* note 8 and Bork, *supra* note 8.

A. *Dealer Services and the Free Rider Problem*

The Court's decision in *Sharp* rested on the assumption that vertical restraints are procompetitive and efficiency enhancing. Proponents of vertical price fixing advance the correlative argument²²² that manufacturers may use vertical restraints to induce dealers to provide important sales services.²²³ Proponents state that the purpose of vertical price fixing is not to raise consumer prices but to increase output, which is economically efficient and procompetitive.²²⁴ Permitting a manufacturer to set a resale price that provides the dealer with a high profit margin consequently induces the retailer to invest in sales services²²⁵ in order to increase sales and realize higher profit margins.²²⁶ As a consequence, the manufacturer realizes both distributive and allocative efficiencies.²²⁷

Closely related to the sales services issue is the problem of discounters "free riding" on the sales and promotion services of full price dealers.²²⁸

222. In addition to motivating a dealer to provide sales services, eliminating the free rider problem, and encouraging new dealer investment in product distribution, the arguments in favor of vertical price fixing are that it protects small dealers, it permits a manufacturer to preserve brand image, and it discourages the use of the product as a loss leader. See S.C. OPPENHEIM, G. WESTON & J.T. MCCARTHY, *FEDERAL ANTITRUST LAWS: CASES, TEXT AND COMMENTARY*, 540-44 (4th ed. 1981). *But see* Pitofsky, *supra* note 98, at 1491-94.

223. 108 S. Ct. at 1520.

224. See, e.g., Bork, *supra* note 8, at 397-405; R. POSNER & F. EASTERBROOK, *ANTI-TRUST: CASES, ECONOMIC NOTES AND OTHER MATERIALS* 211-15 (2d ed. 1981).

225. See Bork, *supra* note 8, at 397-405. Nonprice factors such as services are as important an influence on demand and output as price. Proponents argue that growth in demand and output attributable to the increased services would more than offset the decrease in demand and output due to the higher retail price. *Id.*; see also R. POSNER & F. EASTERBROOK, *supra* note 224, at 211-15.

226. R. POSNER & F. EASTERBROOK, *supra* note 224, at 211-15. Proponents argue, however, that the cost of unrestrained service competition will dissipate additional profits to the point where marginal cost equals price, resulting in maximum distributive efficiency. *Id.*

227. *Id.* Higher profit margins will induce dealers to increase sales services such as advertising, promotion, and in-store demonstrations and displays. *Id.* These pre-sale services will, in turn, increase sales by persuading more consumers to buy the product. *Id.* The increase in economies of scale will reduce per-unit transaction and distribution costs, increasing distributive efficiencies. *Id.* Higher output will allow manufacturers to sell at a price closer to marginal cost and achieve allocative efficiencies. *Id.* *But see* Scherer, *supra* note 98, at 697-705 (arguing that vertical restraints reduce efficiency where competitors' services cancel each other out, where consumers have less choice, and where high prices attract entrants into a saturated market); Comanor, *supra* note 98, at 988-98 (arguing that where all consumers do not demand the same level of services, vertical restraints may not increase efficiency).

228. See Telsler, *supra* note 216, at 91-92. Free riders are dealers that can sell products at discounted prices because they allegedly do not incur the promotional costs associated with a full service dealership. *Id.* The discounter "free rides" on the pre-sale services provided by full service dealers. *Id.* Essentially, these pre-sale services persuade the customer to purchase the product, but, instead of purchasing the product from the full service dealer at the higher price, the customer purchases it from the discounter. *Id.* Since the customer can free ride on

Proponents of vertical price fixing contend that free riding discourages dealers from providing sales services.²²⁹ The free rider can sell at a lower price and take sales away from full service dealers because the free rider does not incur the high costs of sales services.²³⁰ By eliminating price competition, vertical price fixing guarantees dealers the revenues to offset the expense of additional sales services. Moreover, it reduces free riding by allowing manufacturers to either terminate free riders or refuse to supply them.

Opponents of vertical price fixing contend that these efficiencies and procompetitive effects are merely theoretical benefits and that the anticompetitive effects are more pernicious than vertical price fixing proponents indicate. First, they assert that the concept of the "free rider" has never been empirically proven.²³¹ The generalization that discounters offer lower prices because they fail to provide services is unfounded.²³² Discounters often provide sales services that equal or exceed full price retailers' services.²³³ Thus, it is more likely that discounters offer lower prices because they provide these services more efficiently.²³⁴ Vertical price fixing, therefore, prevents more efficient dealers from passing the benefits of their efficiencies to the consumer through reduced retail prices.²³⁵

Second, vertical price fixing protects the inefficient manufacturer from having to compete for dealers and sales on a price basis.²³⁶ Assuring the dealer an adequate profit margin through vertically-fixed prices diminishes the pressure on the manufacturer to reduce prices to dealers in a highly competitive market. The manufacturer may simply terminate the discounter to alleviate the pressure on the wholesale price.

the services of the other dealer, the discounter has no incentive to provide these services and incur the costs. *Id.* Eventually, the full service dealer curtails its promotional services, injuring the manufacturer by reducing sales, and the consumer by reducing competition. *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 55 (1977). *See also* Comanor, *supra* note 98, at 987; Gerla, *supra* note 98, at 3. *See generally* sources cited *supra* note 8.

229. *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 108 S. Ct. 1515, 1520 (1988); Bork, *supra* note 8, at 453-56; Baxter, *supra* note 8, at 21; *see also* Comanor, *supra* note 98, at 987.

230. Bork, *supra* note 8, at 453-56; Baxter, *supra* note 8, at 21; *see also* Comanor, *supra* note 98, at 987.

231. Shores, *Vertical Price-Fixing and the Contract Conundrum: Beyond Monsanto*, 54 *FORDHAM L. REV.* 377, 401-04 (1985).

232. Gerla, *supra* note 98, at 4.

233. *Id.*

234. Pitofsky, *supra* note 98, at 1493; *see also* R. STEINER, *infra* note 249, at 3, 13-21. The large markups of full price retailers are often due to inefficient operations and practices such as poor space and labor utilization, excessive advertising, overcapacity, bundling of sales services rather than charging for services based upon use, and high transaction and other overhead costs. Gerla, *supra* note 98, at 4-5.

235. *See* Gerla, *supra* note 98, at 4-5.

236. Pitofsky, *supra* note 98, at 1490-91.

Third, to the extent vertical price fixing induces services, it does so inefficiently.²³⁷ It does not guarantee the level or types of services that the manufacturer desires or needs. In fact, it does not guarantee that the dealer will provide any services at all. A services requirement in the dealer agreement provides a more efficient and less restrictive means of assuring an appropriate level and type of service from a dealer.²³⁸ The dealer's failure to supply the contractually required services would result in a breach of the dealer agreement and a justifiable termination of the violating dealer.

Inefficiencies also result from a system that removes the price/product/service mix determination from the market.²³⁹ The assumption that the manufacturer knows better than the market the appropriate level and mix of services, and the price that would achieve them, does not comport with the lessons of competitive market economics. A system that allows consumers to choose between different price/product/service mixes and gives the dealer the flexibility to respond to these demands more efficiently allocates resources.²⁴⁰

Finally, the argument that vertical price fixing eliminates the free rider problem provides only weak justification. Because a vertical price fixing system imposes no obligation to provide a certain level or type of service, a dealer will always find it more profitable to "cheat" by reducing the level of sales services it provides and riding free on the services of other dealers.²⁴¹ Again, a sales services provision in the dealer agreement more efficiently and less restrictively assures that alleged free riders provide the level and type of service that the manufacturer deems necessary.²⁴²

B. Attracting New Dealers to Invest in Distributing the Product

The *Sharp* Court noted that vertical restraints have the potential to induce competent and aggressive retailers to invest in the capital and labor needed to distribute a product more efficiently.²⁴³ Proponents of vertical price fixing also advance this argument in support of their view. Vertical price fixing

237. *Id.* at 1493.

238. *Id.*

239. *Id.*

240. *Id.*

241. Halverson, *supra* note 180, at 64.

242. *Id.* The manufacturer structures the agreement with the dealer to assure that certain services are provided in line with the manufacturer's promotional needs and the customer's informational needs. Without a vertical price fixing agreement, the dealer has the flexibility to adjust his price to a level that takes advantage of any efficiencies in the provision of these services. *Id.*; see also Pitofsky, *supra* note 98, at 1493.

243. *Sharp*, 108 S. Ct. at 1519-20; *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 55 (1977).

provides an incentive, in the form of a higher profit margin, to attract new dealers to invest in a product's distribution.²⁴⁴ Increasing the number of dealers provides the consumer with more choice and more product information, thereby increasing distributive efficiency and enhancing consumer welfare.²⁴⁵

Opponents argue that vertical price fixing is not needed to attract new dealers and may even reduce efficiency.²⁴⁶ In a market characterized by low sales and high demand potential, the manufacturer wants to attract new dealers to invest in distribution in order to realize this potential. However, allowing the manufacturer to raise the price to consumers to attract new dealers generates considerable controversy.²⁴⁷ A more economically efficient solution would compel a manufacturer to compete for new dealers by lowering wholesale prices.²⁴⁸

Opponents also contend that vertical price fixing hinders the expansion and survival of new businesses. The survival of a new business often depends on its ability to exploit any cost advantages by cutting prices in order to attract and develop a customer base.²⁴⁹ Vertical price fixing removes pricing discretion and, consequently, reduces the ability of new retailers to attract customers. Eliminating price competition as a marketing strategy may contribute to the demise of many new businesses.²⁵⁰ The high number of business failures, the low rate of business start-ups, and high consumer prices during the fair trade period demonstrate this potential.²⁵¹

Attracting new dealers into a demand-saturated market may be inefficient. Demand for the product does not increase, but instead shifts from one new dealer to another. "Competitors' services simply cancel each other out" and the dealers cannibalize each other's sales.²⁵² In addition, as sales are reallocated among more dealers in a saturated market, dealers lose economies of

244. See Posner, *Antitrust Policy and the Supreme Court: An Analysis of the Restricted Distribution, Horizontal Merger and Potential Competition Decisions*, 75 COLUM. L. REV. 282, 283-85 (1975).

245. See R. BORK, *supra* note 8, at 288-91, 297-98.

246. See Pitofsky, *supra* note 98, at 1494; Scherer, *supra* note 98, at 704-05.

247. Pitofsky, *supra* note 98, at 1494.

248. *Id.*

249. See R. STEINER, VERTICAL RESTRAINTS AND ECONOMIC EFFICIENCY 14, 17-18 (Federal Trade Commission Working Paper No. 66, June 1982).

250. *Hearings, supra* note 13, at 105 (statement of Mr. Monroe G. Milstein, Chairman of Burlington Coat Factory, citing 1975 Justice Department Study). See also S. REP. NO. 466, *supra* note 13, at 3, reprinted in 1975 U.S. CODE CONG. & ADMIN. NEWS 1569, 1571-72.

251. See S. REP. NO. 466, *supra* note 13, at 3, reprinted in 1975 U.S. CODE CONG. & ADMIN. NEWS 1569, 1571-72.

252. Scherer, *supra* note 98, at 704.

scale.²⁵³ Resources are allocated less efficiently when vertical price fixing coaxes new dealers into a market where demand volume has reached its maximum.

C. Vertical Price Fixing and Cartelization

The *Sharp* Court noted that vertical price fixing could reduce interbrand competition by facilitating cartelization.²⁵⁴ However, it dismissed the cartelization issue because no evidence demonstrated the cartelizing effects of nonprice restraints.²⁵⁵ In mischaracterizing the issue as a nonprice restraint, the Court incorrectly disposed of the cartelization issue.

Commentators on both sides of the vertical price fixing debate recognize the dangers that cartelization poses in a vertical price fixing environment.²⁵⁶ Proponents note, however, that a number of factors mitigate the dangers of cartelization. First, a cartel is difficult to hold together.²⁵⁷ Cartels are expensive and difficult, if not impossible, to coordinate and police.²⁵⁸ In addition, if entry into the market is relatively easy, vertical price restraints are unlikely to facilitate cartelization.²⁵⁹ Thus, a cartel will succeed only in highly concentrated markets where a small number of manufacturers and dealers account for most of the sales in the area.²⁶⁰

Proponents also contend that the per se proscriptions against cartelization or price fixing at the manufacturers' or dealers' levels provide adequate protection against cartelizing behavior. As the majority noted in *Sharp*, anti-trust law focuses primarily on interbrand competition, not intrabrand competition.²⁶¹ Because the per se proscription against horizontal price fix-

253. *Id.* at 704-05.

254. *Sharp*, 108 S. Ct. at 1520.

255. *Id.*

256. Scherer, *supra* note 98, at 691-92. Proponents have noted this danger. *Sharp*, 108 S. Ct. at 1520; Posner, *supra* note 244, at 294; GUIDELINES, *supra* note 12, at 16-18. Opponents of vertical price fixing have also recognized it. Halverson, *supra* note 180, at 6466; Pitofsky, *supra* note 61, at 15-17.

257. *Sharp*, 108 S. Ct. at 1521.

258. *Id.*

259. GUIDELINES, *supra* note 12, at 16-18. Entry of new manufacturers and dealers would undermine the cartel by cutting prices. Substitute products also put price pressure on cartels unless the manufacturers of those substitutes also participate in the cartel. *Id.*

260. *Id.*

261. *Sharp*, 108 S. Ct. at 1520. Vertical restraints decrease intrabrand competition by reducing the number of distributors of the same product in a particular location, restricting the customers to whom a dealer may sell, requiring exclusive dealership arrangements, or by fixing the price at which a dealer may resell the product. Proponents contend, however, that interbrand competition provides a significant check on the ability of the manufacturer or dealer to exploit intrabrand market power due to the availability of competitors' products. See *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 54-55 (1977).

ing adequately protects interbrand competition, the per se rule against vertical price fixing is not needed.

Opponents of vertical price fixing find these arguments unpersuasive. In their view, permitting vertical price fixing would facilitate the creation and stabilization of interbrand manufacturer cartels and, thereby, reduce interbrand competition. First, they argue that proponents of vertical price fixing attach too much weight to the assumption that distribution markets are perfectly competitive.²⁶² In general, interbrand competition is overestimated as a check on cartelization. Brand or product imaging differentiates similar products and reduces competition among these products.²⁶³ Manufacturers may impose nonprice vertical restraints, such as territorial or customer restrictions or exclusive dealing arrangements, which effectively limit the amount of interbrand as well as intrabrand competition.²⁶⁴ They may likewise terminate dealers for non-compliance with these restraints. All of these factors increase concentration in the market and facilitate cartelization.

Second, if the impetus for an action that promotes vertical price fixing comes from a dealer, it is more likely that the purpose is to suppress price competition, and its effect is to facilitate a cartel.²⁶⁵ Even proponents of vertical price fixing admit that the imposition of vertical restraints in response to the demands or complaints of dealers is more likely to be anticompetitive and inefficient than those imposed based on the independent judgment of a manufacturer.²⁶⁶ The manufacturer's independent decision to impose vertical restraints more likely attempts to enhance distributive efficiencies and increase output.²⁶⁷ Dealers are more concerned with competition and profit margin than with distributive efficiencies,²⁶⁸ and their complaints about discounting dealers are more likely intended to further a horizontal agreement.²⁶⁹ Where a complaint results in the termination of a dealer, the restraint takes on the character of a horizontal restraint of trade and should be classified as such regardless of the number of parties involved in the boycott.²⁷⁰ In determining whether a particular restraint of trade is

262. Gerla, *supra* note 98, at 18.

263. *Id.*

264. See, e.g., Pitofsky, *supra* note 61, at 27-38 (arguing that vertical restrictions other than vertical price fixing can be highly anticompetitive and reduce the ability of discounters to compete); Gerla, *supra* note 98, at 16, 23-25 (certain vertical restraints are as damaging to competition as vertical price fixing).

265. Campbell & Ware, *Russell Stover and the Vertical Agreement Puzzle*, 52 ANTITRUST L.J. 83, 89 (1989); see also Pitofsky, *supra* note 98, at 1490-91.

266. R. POSNER, ANTITRUST LAW: AN ECONOMIC PERSPECTIVE 148, 165 (1976).

267. *Id.*

268. Campbell & Ware, *supra* note 265, at 89.

269. *Id.* at 89.

270. Gerla, *supra* note 98, at 9-10.

unreasonable, the substance and effect of the restraint should carry more weight than its form.

Finally, manufacturers organizing and enforcing dealer cartels diminish pressure on their own wholesale prices and therefore, stabilize interbrand manufacturer cartels.²⁷¹ Retail prices are much more visible and public and can be used by manufacturers as a measure of their competitors' compliance with a cartel agreement.²⁷² Providing dealers with a guaranteed return reduces the pressure on a manufacturer to lower prices, reduces incentives to become more efficient and, thus, facilitates cartelization and fosters inefficient behavior.²⁷³ Price competition is reduced and nonprice factors such as services, advertising, and promotion take over, creating an illusion of intense competition.

V. CONGRESSIONAL PROPOSAL TO CODIFY THE PER SE STANDARD

Congressional concern about the impact of the *Monsanto* decision on private vertical price fixing actions resulted in the House of Representatives' passage of the Freedom from Vertical Price Fixing Act²⁷⁴ of 1987. That same year, the Senate Judiciary Committee passed the Retail Competition Enforcement Act²⁷⁵ of 1987 and submitted it to the Senate for approval. Neither bill passed in the 100th Congress, but both were reintroduced in the 101st Congress.²⁷⁶ The measure²⁷⁷ would amend the Sherman Antitrust Act and, as proposed, would accomplish several purposes.

First, the proposal would codify the per se rule against vertical price fixing. It would make clear that all forms of vertical price fixing are illegal, and evidence of an agreement on a specific price or price levels would not be required to prove a vertical price fixing conspiracy.²⁷⁸ Thus, a court would

Whether a boycott is implemented by a single competitor or a group of competitors should make no difference in the treatment of the tactic under the antitrust laws. A boycott sponsored by a single, influential competitor can be just as devastating to a discounter and the competition it provides as can a boycott sponsored by a group of competitors.

Id. at 10. The suppression of competition by an illegal act is the essence of a section 1 Sherman Act violation. Nowhere does the Act require a minimum number of parties for the illegal conduct to constitute a violation of section 1. *Id.*

271. See Pitofsky, *supra* note 61, at 16-17.

272. See Shores, *supra* note 231, at 402-03.

273. See Pitofsky, *supra* note 61, at 16-17.

274. H.R. 585, 100th Cong., 1st Sess. (1987).

275. S. 430, 100th Cong., 1st Sess. (1987).

276. See *supra* note 171.

277. Because both laws would accomplish the same purposes, this Note analyzes the House of Representative's version.

278. H.R. REP. NO. 421, *supra* note 15, at 38. In codifying the per se standard, Congress would unequivocally affirm its support of the standard and reject as a matter of legislative

find a violation of the Sherman Act where a manufacturer and supplier conspired either to fix or maintain prices, to restrict another dealer's ability to determine his resale price, or to terminate or cut off supply to a price-cutter.²⁷⁹ The proscription would be absolute, covering all activity designed "to restrain price movement and the free play of market forces."²⁸⁰

Second, the revised measure would reverse the *Monsanto* and *Sharp* evidentiary standard. It would properly return to the trier of fact the task of determining whether a set of facts indicates the existence of concerted action or agreement.²⁸¹ Specifically, the jury would determine whether the plaintiff presented sufficient evidence to infer a contract, combination, or conspiracy to set, change, or maintain prices in violation of the Sherman Act.²⁸² The plaintiff would not be required to present evidence sufficient to show an explicit agreement on prices or price levels in order to reach the jury.²⁸³

Third, the measure details the type of evidence that would be sufficient to meet the new evidentiary standard; that is, a communication between a manufacturer and a dealer regarding price competition.²⁸⁴ Under the proposed statute, to reach the trier of fact the plaintiff must show only the existence of price communications. It defines a price communication as any express or implied threat, suggestion, request, or demand from the manufacturer or rival dealer that the plaintiff discontinue price competition.²⁸⁵ Moreover, the statute would require the plaintiff to show that the termination or refusal to supply was "in response to" such demands or threats from the supplier.²⁸⁶ A termination "following" a complaint would not imply causation.²⁸⁷

policy "recent efforts to qualify, trivialize, or dilute the breadth of the RPM (resale price maintenance) stricture." *Id.* The new version of section 2 would reverse the impact of the *Sharp* decision by deeming vertical price fixing agreements illegal per se whether or not a specific price level is agreed upon. *See* H.R. 1236, 101st Cong., 1st Sess. (1989).

279. H.R. REP. NO. 421, *supra* note 15, at 38. The bill attempts to eliminate the "artful" blurring of the distinction between nonprice and price restraints, currently practiced by some courts and the administration, by concentrating on the purpose and effect of the conduct. *Id.* at 38-39. That is, if the purpose and effect of the conduct is to stifle price competition in any manner, then vertical price fixing is implicated and the per se rule would apply. *Id.* at 39.

280. *Id.* (quoting *Cernuto v. United Cabinet Corp.*, 595 F.2d 164, 169 (3d Cir. 1979)).

281. *Id.* at 31-32.

282. *Id.* Communications between manufacturers and dealers concerning price competition that result in the termination of the price cutter, would constitute a sufficient showing of causation to reach a jury. The plaintiff need not disprove that the manufacturer acted independently. *Id.*

283. *See supra* note 278.

284. H.R. REP. NO. 421, *supra* note 15, at 26-27, 31.

285. *Id.* at 34-35.

286. *Id.* at 31. "In response to" a complaint implies a causal relation to the price communication. *Id.*

287. *Id.*

Finally, the plaintiff would be required to convince the trier of fact that these demands or threats were the major or substantial contributing cause of its termination.²⁸⁸ If such evidence was available, the court would be required to present the issue to the jury.²⁸⁹

VI. CONCLUSION

While the *Sharp* Court left the per se rule against vertical price fixing intact, it continued the trend of the Court's holdings in *Sylvania* and *Mon-santo*, by narrowing the scope of the absolute prohibitions against vertical restraints. By adopting the Chicago School and Reagan administration position that vertical restraints are procompetitive and efficiency enhancing the Court has effectively repudiated the Congressional position on vertical price fixing, and has quite likely set the stage for overturning *Dr. Miles*. The Court's commitment to the holding of *Dr. Miles* appears to rest solely on the doctrine of stare decisis.

The legal and economic impact of *Sharp* is predictable. Discounters have much less legal protection against collusive termination. *Sharp* has further reduced the likelihood of bringing a successful vertical price fixing action and, therefore, will result in an increase in dealer terminations.

Economic experience proves that vertical price fixing results in higher prices to the consumer. However, no empirical evidence demonstrates that higher prices result in better sales services. The *Sharp* decision rests solely on an economic theory propounded by the Chicago School and supported by the Reagan administration. Nothing in the *Sharp* holding guarantees that the quantity or quality of consumer sales services will improve after *Sharp*. If a manufacturer determines that the provision of sales services would increase output, a dealer contract would provide a much less restrictive means to secure the services from the retailer. Vertical price fixing is an economically inefficient means of inducing these services and, except for a few well defined exceptions, it is purely a means of transferring wealth from consumers to manufacturers and dealers.

The proposed amendment to the Sherman Act offers the only means of assuring that consumers and discounters will be protected from the real and damaging consequences of a practice affording only illusory benefits. Congress should act to preserve competition that will benefit both consumers

288. *Id.* at 33. The evidentiary burden has been equated to a "but for" causation test such that de minimis or immaterial causation does not raise an inference. *Id.* at 33-34.

289. *Id.* at 32. Such evidence would be sufficient to overcome a motion for summary judgment, directed verdict, or judgment notwithstanding the verdict. However, the defendant is not precluded from submitting evidence that rebuts the plaintiff's evidence and thereby obtain a summary judgment, directed verdict or judgment notwithstanding the verdict. *Id.* at 32-33.

and manufacturers in the long run by making manufacturers more competitive and efficient. Although antitrust laws protect competition, not competitors, Congress must act to protect a certain class of competitors, the discounters. If no action is taken to protect discounters, competition will certainly be reduced, resulting in higher prices and lower output.

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