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THE ANTITRUST CONSEQUENCES OF MANUFACTURER-SUGGESTED RETAIL PRICES—THE CASE FOR PRESUMPTIVE ILLEGALITY

William R. Andersen*

I. INTRODUCTION

Contemporary marketing bristles with antitrust implications. One cluster of marketing strategies involves the attempts of manufacturers to control the distribution of their products. When successful, such efforts impose constraints upon those who are placed “vertically” down the distribution chain—wholesalers, jobbers, retail dealers, etc.¹ The range of vertical control which may be used by a manufacturer includes control over the territories within which its reselling dealers can operate, control over the customers to whom its dealers are permitted to sell, control over the range of its product line any particular dealer will (or must) carry, control over what other competing products its dealers may also carry, control over which individuals will be selected as dealers, and, of course, control over the price at which its product will be resold. The techniques by which such control is exercised will vary with the matter at hand. The controls also will vary in formality from express agreements and undertakings by the dealer to informal pressures and “persuasions” not committed to writing or even, for that matter, to words.²

The courts have varied in their treatment of manufacturer efforts to impose *nonprice* controls on product distribution. In 1963, the first Supreme Court consideration of the question³ indicated that the Court would appraise vertical nonprice constraints under the rule of reason,

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1. To simplify the discussion in this article it will be assumed that the distribution system involves only two tiers—the manufacturer and the retail dealer. The central concern of this article is suggested *retail* prices, a part of the broader theoretical area of suggested *resale* prices.

2. For a general discussion of the techniques of vertical control in distribution, with special references to price controls, see B. YAMEY, *THE ECONOMICS OF RESALE PRICE MAINTENANCE* (1954); Bowman, *The Prerequisites and Effects of Resale Price Maintenance*, 22 U. CHI. L. REV. 825 (1955); Keck, *Alternative Distribution Techniques—Franchising, Consignment, Agency, and Licensing*, 13 ANTITRUST BULL. 177 (1968); Tester, *Why Should Manufacturers Want Fair Trade?*, 3 J. LAW & ECON. 86 (1960).

3. *White Motor Co. v. United States*, 372 U.S. 253 (1963).

rather than condemn them as per se offenses.⁴ Counseling, advocacy and decisionmaking proceeded therefore through an evaluation of the harms and benefits of an arrangement to determine if, on balance, the restraint was unreasonable.⁵ Four years later in *United States v. Arnold, Schwinn & Co.*,⁶ the Court reversed its position and held that so long as the manufacturer actually sold the product to the dealer, any efforts to control territories within which the dealer sold, or customers to whom he sold, were per se offenses of the antitrust laws. The opinion was much criticized⁷ and only indifferently followed by lower courts.⁸ In 1977, the Court again reversed direction in *Continental T.V., Inc. v. GTE Sylvania, Inc.*⁹ The Court indicated that the per se rule was too abrupt a way of dealing with at least some nonprice restrictions. At present, commentators and other courts are at work purifying the implications of *Sylvania*.¹⁰

The attitude of the courts toward vertical *price* restraints has been more consistent. From the earliest decision in 1911¹¹ through the 1977 *Sylvania* opinion, the Court has regularly declared that vertical price fixing is a per se offense.¹² Ignoring the ten years when *Schwinn* was in full sway, it could be said that the courts have generally subjected vertical nonprice restraints to rule of reason appraisal, but have condemned vertical price restraints under the per se rule. Although this conclusion appears to be consistent with the cited cases, it misdescribes the practical effect of the doctrine. The criteria used to determine what constitutes

4. The conventional dichotomy between the presumptive illegality of the per se approach and the more elaborate inquiry involved in the rule of reason approach is summarized in L. SULLIVAN, HANDBOOK OF THE LAW OF ANTITRUST 165-86 (1977). A short statement of the approaches as they are applied to vertical restrictions may be found in Pitofsky, *The Sylvania Case: Antitrust Analysis of Non-Price Vertical Restrictions*, 78 COLUM. L. REV. 1 (1978).

5. See Comanor, *Vertical Territorial and Customer Restrictions: White Motor and Its Aftermath*, 81 HARV. L. REV. 1419 (1968).

6. 388 U.S. 365 (1967).

7. See, e.g., Baker, *Vertical Restraints in Times of Change: From White to Schwinn to Where?*, 44 ANTITRUST L.J. 537 (1975); Handler, *The Twentieth Annual Antitrust Review—1967*, 53 VA. L. REV. 1667 (1967); Posner, *Antitrust Policy and the Supreme Court: An Analysis of the Restricted Distribution, Horizontal Merger and Potential Competition Decisions*, 75 COLUM. L. REV. 282 (1975); Robinson, *Recent Antitrust Developments: 1974*, 75 COLUM. L. REV. 243 (1975).

8. The cases are reviewed in Robinson, *supra* note 7, at 270-81.

9. 433 U.S. 36 (1977).

10. Of special interest in the voluminous *Sylvania* literature are Louis, *Vertical Distribution Restraints After Sylvania: A Postscript and Comments*, 76 MICH. L. REV. 265 (1977), and Pitofsky, *supra* note 4.

11. *Dr. Miles Medical Co. v. John D. Park & Sons*, 220 U.S. 373 (1911).

12. Mr. Justice Powell, writing for the Court in *Sylvania*, conceded that some commentators urged that vertical price and nonprice restrictions should be judged by the same criteria, but nevertheless explicitly retained the per se rule for price restrictions on the basis of long standing judicial authority, economic effects, and Congressional policy. 433 U.S. at 51 n.18.

vertical price fixing are less stringent than the criteria used to characterize price-related conduct among horizontal competitors.¹³ As a result, a substantial range of conduct which would clearly be regarded as price fixing if the participants were horizontally related is regarded as something less than price fixing when the relationship is vertical. Much vertical conduct affecting price thus is exempt from the per se rule, and indeed, from antitrust scrutiny altogether.

A manufacturer's suggestion of resale prices to dealers is an example of price-affecting conduct which is said to create no antitrust liability despite the fact that liability would result from identical conduct if the parties were horizontally related. This article argues that permitting parties to tamper with the price term in any fashion risks contravention of the policies behind the antitrust laws, and that making the antitrust consequence turn on whether the parties appear to be related vertically or horizontally is not an intelligible way of minimizing that risk. In conclusion it is recommended that suggested prices should be presumptively illegal. Because this recommendation is a significant departure from prevailing doctrine, it will be helpful to note first the techniques by which vertical conduct affects resale prices, and then to sketch the history of legal doctrine relating to that conduct.

II. THE LAW AND PRACTICE OF VERTICAL CONDUCT AFFECTING PRICE

A. *Manufacturer Conduct Affecting Resale Price*

The manufacturer interested in affecting the resale price of its product has a variety of ways to communicate its preference to dealers. The most direct method is to negotiate a contract which obligates the dealer to resell at a fixed price, or at least not to undercut a stated price.¹³ Ordinarily, such formal agreements are banned,¹⁴ but the development of marketing arrangements with a prospective dealer still provides ample opportunity for the manufacturer to express its preference as to resale price. For example, a less direct but equally efficient means of transmitting information to the dealer about the manufacturer's preference is through catalogs and price lists. Often, such catalogs and lists will identify the

13. The basic concern of this article is manufacturer control of minimum dealer prices, since this impedes vigorous dealer competition. Manufacturer control of maximum dealer prices presents quite a different economic issue, although the courts have not distinguished between the two forms of price control. See *Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211 (1951); L. SULLIVAN, *supra* note 4, at 210-12, 390-91.

14. See Part II-B *infra*.

retail price of the product, with the dealer's price being calculated as a percentage discount off the stated retail price.¹⁵

Another common technique is for the manufacturer to aid the dealer in dealer advertising in a manner which affects pricing. The manufacturer may, for example, provide advertising displays, window cards, newspaper mats and other forms of advertising which picture or describe the product and which include its retail price. Although a dealer who uses such advertising is technically free to sell at a lower price, it is unlikely that a dealer would do so; one would ordinarily advertise one's lowest price. The manufacturer may make provision for some form of joint advertising allowance to the dealer, conditioning the manufacturer's contributions upon the dealer's refraining from advertising the product at a lower price than the manufacturer has suggested.¹⁶ A further variation is for the manufacturer itself to advertise in local, regional, or national publications and media, stating the retail price in such advertisements. Although such manufacturer advertising is not conduct which directly involves the dealer, it does serve as a channel through which manufacturer pricing preferences are communicated to both dealers and consumers. Conceivably, through the use of trade publications, some price information can be transmitted to the dealer by advertising or news stories without informing the public.

Finally, manufacturers may include with or imprint on the product some indication of its retail price. This may be part of the art work in which the product is dressed and may be either inseparable from the package or detachable. Detachment may be easy or difficult, noticeable or not. The price information may also be part of the warranty or instructional material included with the product which cannot easily be removed from the product.

In all of these transmissions, the price may be stated in clear and unambiguous terms or it may be in a code only the dealer can read. The price may be stated with varying degrees of precision, ranging from

15. There may be an independent need for such catalogs and lists—beyond their function as transmission belts for manufacturer pricing preferences. With some product lines, for example, the number of separate items to be priced or the complexity of their combinations may make it highly useful to the retailer to have this information calculated and identified for him, quite apart from any value that either the retailer or the manufacturer may perceive in the level of prices as such. Further, there may be greater or lesser degrees of knowledge about whether all other retailers receive the same catalogs and price lists, just as there will be variations in the extent to which consumers will have access to these data.

16. See *P.D.Q., Inc. v. Nissan Motor Corp.*, 577 F.2d 910 (1978); *The Advertising Checking Bureau, Inc.*, 2 TRADE REG. REP. (CCH) ¶ 21,540 (1979) (consent order).

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"About \$9.95" or "Less than \$10.00" to "Suggested Retail Price, \$9.95" or "Manufacturer's Suggested Retail Price, \$9.95."¹⁷

B. Legal Doctrine Surrounding Suggested Resale Prices

Section 1 of the Sherman Act prohibits any "contract, combination . . . , or conspiracy, in restraint of trade."¹⁸ The following discussion examines the two components of the statutory offense: that the defendant's conduct must restrain trade in the statutory sense, and that there must be some joint effort or "agreement."¹⁹

1. Conduct in restraint of trade

Some conduct is deemed so typically harmful to competition and so devoid of credible benefits as to be presumed unlawful under section 1 without any proof of the defendant's power or purpose, or without extensive inquiry into the effects of the arrangement. Of these per se offenses, price fixing is the clearest and most consistent example. Other conduct, thought to be harmful to competition only under certain circumstances or thought to involve substantial benefits, is said to be judged by a rule of reason;²⁰ such conduct is condemned only if an analysis of the defendant's market power and purpose and the likely effect of the arrangement shows that it will produce more harms than benefits.

The first vertical price fixing case to reach the Supreme Court, *Dr. Miles Medical Co. v. John D. Park & Sons Co.*,²¹ was decided in 1911.

17. This brief catalog of techniques inevitably suggests that the price information is flowing down from the manufacturer to the dealer and that in turn suggests that it is the manufacturer's interest which is being served by the transmission. Yet, it is not at all obvious why the manufacturer should be interested in keeping up the retail price of his product. In theory, the manufacturer's price to the dealer (and hence its profit on each unit) remains the same whatever price the dealer charges to his customer. Since the lower the dealer's price, the greater quantity of the product is likely to be sold, it would appear to be in the manufacturer's interest to encourage the reduction of retail prices in order to maximize sales. The manufacturer, in short, should favor retail price cutting, not fight it, because the lower the retailer's margin the greater the manufacturer's profits.

Two kinds of explanations have been given for the continuation of manufacturer efforts to control retail prices in the face of the apparent economic harm done to manufacturers by increased retail prices. One response is that the phenomenon is essentially retailer-inspired because "resale price maintenance" serves retailer interests in reducing intrabrand competition. The other answer is that there are in fact benefits to the manufacturer from the support of resale prices. Both of these responses will be examined after the legal setting has been described. See Part III *infra*.

18. 15 U.S.C. § 1 (1976).

19. See Part II-B *infra*. The classic consideration of the requirement of an agreement is Turner, *The Definition of Agreement under the Sherman Act: Conscious Parallelism and Refusals to Deal*, 75 HARV. L. REV. 655 (1962).

20. See generally L. SULLIVAN, *supra* note 4, at 165-86.

21. 220 U.S. 373 (1911).

Dr. Miles was a manufacturer of patent medicines which were sold to wholesale drug companies for distribution through retail drug stores. Dr. Miles had formal contracts with over 400 wholesalers and 25,000 retail dealers in the United States; the effect of these contracts was to fix the retail price charged the consumer. In an action involving one of these contracts, the circuit court ruled that the contracts were in restraint of trade and void. The Supreme Court affirmed. The defendant had contended that because it could sell or not as it chose, it could also attach any conditions it pleased to the sale, including conditions under which its buyer could resell. Justice Hughes, writing for the majority, rejected this argument, and laid down what is still the basic law of vertical price restraints.

Three aspects of the *Dr. Miles* opinion are of special interest in this analysis. First, in finding the contracts illegal, Hughes relied on the principles of unlawful restraints on alienation which prohibit a manufacturer from unduly restricting a buyer's selling options. The language of the opinion shows its kinship with the restraints on alienation cases and the principle that emerges is much like a rule of reason standard:

To sustain the restraint, it must be found reasonable both with respect to the public and to the parties, and that it is limited to what is fairly necessary . . . for the protection of the covenantee. . . . The question is whether, under the particular circumstances of the case and the nature of the particular contract involved in it, the contract is or is not, unreasonable.²²

This restraint on alienation analysis suggests that one value Hughes saw reflected in the Sherman Act was freedom for the dealer to make its own pricing decisions without manufacturer interference.

Second, although the Court did not prohibit the contracts on the ground that vertical price fixing was a per se offense, there is nevertheless a per se mood in the opinion. Hughes briskly and negatively characterized the purpose of the arrangement as being "designed to maintain prices . . . [of] the articles, and to prevent competition among those who trade in them."²³ He then dismissed asserted justifications based on the character of the commodity, the degree of restriction, and the character of prior ownership.²⁴ The recent *Sylvania* case shows that the Court continues to subject vertical price restraints to an especially intense antitrust scrutiny.²⁵

A third important aspect of the opinion is the recognition that horizon-

22. *Id.* at 406.

23. *Id.* at 407.

24. *Id.* at 408-09.

25. See note 12 and accompanying text *supra*.

tal effects on competition may result from vertical price maintenance arrangements. Hughes concluded that because the agreement had the effect of preventing competition among retailers it should be judged on the same basis as an agreement between horizontally related competitors;²⁶ the focus was thus on the effects rather than the asserted purpose when the two did not coincide. The Court recognized that benefits might flow from the vertical arrangement, but Hughes concluded that such benefits accrued primarily to the retailer,²⁷ and that even if there were benefits to the manufacturer, they could not be used to justify an arrangement which foreclosed horizontal competition. He wrote that once the manufacturer "sold its product at prices satisfactory to itself, the public [was] entitled to whatever advantage may be derived from competition in the subsequent traffic."²⁸

Although *Dr. Miles* did not explicitly hold that vertical price fixing was a per se offense, that rule was quickly adopted once *United States v. Trenton Potteries Co.*²⁹ established a per se rule against horizontal price fixing. In later cases, the Court said vertical price fixing was prohibited by the Sherman Act regardless of the commodity involved,³⁰ the market power of the manufacturer,³¹ and the existence of the significant benefits

26. 220 U.S. at 407-08. The court stated:

If there be an advantage to the manufacturer in the maintenance of fixed retail prices, the question remains whether it is one which he is entitled to secure by agreements [of this sort] As to this, the [manufacturer] can fare no better . . . than could the dealers themselves if they formed a combination and endeavored to establish the same restrictions

[A]greements or combinations between dealers, having for their sole purpose the . . . fixing of prices, are injurious to the public interest and void. They are not saved by the advantages which the participants expect to derive

Id.

27. *Id.* at 407. Justice Hughes has been much criticized for the *Dr. Miles* opinion. It is said that he was too abrupt in judging this kind of price fixing in that he failed to recognize that manufacturers have legitimate interests in the control of resale prices. As has been indicated, however, Hughes did not deny the existence of such benefits. He merely said they did not justify the conceded harms. Perhaps closer to the mark, Hughes did not perceive what are today seen as the benefits to competition which are said to flow from some kinds of vertical restraints. He treated asserted benefits of the restraints as windfalls to the manufacturer and hence not weighty in the antitrust calculus—especially when balanced against the harms of eliminating intrabrand competition. Moreover, the suggestion that Hughes was unusually hostile to price fixing seems difficult to square with the historical record. As counsel, he did, after all, represent the Colgate Company in the litigation which substantially limited *Dr. Miles*. He was counsel for Trenton Potteries in 1927, urging the Court (unsuccessfully this time) to adopt the rule that reasonable price fixing was not a violation of the Sherman Act. See note 29 and accompanying text *infra*. And when Hughes returned to the Court, it was he who wrote the decision in *Appalachian Coals, Inc. v. United States*, 288 U.S. 344 (1933), which permitted the application of a rule of reason to a form of price fixing. He was hardly a justice one could accuse of being unsympathetic to the possible benefits of price fixing.

28. 220 U.S. at 409.

29. 273 U.S. 392 (1927).

30. See, e.g., *United States v. Line Material Co.*, 333 U.S. 287, 307 (1948).

31. See, e.g., *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305 (1956).

to the manufacturer, including those protected by patents and copyrights.³² Resale price maintenance also was held to be an unfair method of competition under the Federal Trade Commission Act.³³

2. *Agreement between the parties*

Because the arrangement in *Dr. Miles* involved an express agreement between the manufacturer and the wholesalers and dealers, no issue was raised about the second component of a Sherman Act offense: whether there was a "contract, combination, or conspiracy." Nor did the Court consider what conduct short of explicit price fixing should be included within the ban. These issues, in strangely tangled form, arose a few years later in *United States v. Colgate & Co.*³⁴

The case arose from a criminal indictment alleging that Colgate was engaged in an unlawful conspiracy to fix resale prices. Colgate's allegedly conspiratorial conduct included notifying its dealers about appropriate resale prices, urging their adoption, threatening to cut off dealers who did not cooperate, asking for information about dealers who were not complying with the company's requests, and seeking assurances from dealers that the suggestions would be complied with.³⁵ Today, these allegations would be clear evidence of an "agreement." Nonetheless, in an ambiguous interpretation of the indictment, the trial court had sustained the defendant's demurrer. The Supreme Court affirmed, finding that "as interpreted below, the indictment does not charge Colgate . . . with selling its products to dealers under agreements which obligated the latter not to resell except at prices fixed by the company."³⁶

With the issue of agreement thus resolved, any liability would have to have been predicated on Colgate's completely unilateral action in cutting off dealers with whom it no longer chose to do business, a position neither court would accept. The trial court held that the manufacturer had an "undoubted right to decline to further deal"³⁷ with customers who refused to resell at the understood price. The Supreme Court agreed that liability would not attach under these circumstances, and the following language from its opinion has governed the law of suggested retail prices for sixty years:

32. L. SULLIVAN, *supra* note 4, at 377.

33. *FTC v. Beech-Nut Packing Co.*, 257 U.S. 441 (1922).

34. 250 U.S. 300 (1919).

35. *Id.* at 303.

36. *Id.* at 307.

37. *Id.* at 305.

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In the absence of any purpose to create or maintain a monopoly, the act does not restrict the long recognized right of a trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal.³⁸

In exercising that "long recognized right," the manufacturer is free to "announce in advance the circumstances under which he will refuse to sell."³⁹ Presumably, one of the permitted "circumstances" is a refusal by the dealer to continue to charge the resale price suggested by the manufacturer.

The effect of *Colgate*, of course, is not directly to approve resale price maintenance by manufacturers; by its terms the case only protects the manufacturer's power to terminate dealers. The result nevertheless allows the manufacturer to discipline dealers who do not comply with its pricing preference. Hence, the case confers broad antitrust immunity on much manufacturer conduct aimed at controlling resale prices. The Court did not retreat openly from the policy against vertical price fixing announced in *Dr. Miles*.⁴⁰ The Court instead reached this result by placing a special emphasis on the technical element of "agreement." The opinion implies that so long as the arrangement between the manufacturer and the dealer does not impose a legal duty on the dealer to comply with the manufacturer's pricing suggestions, there is no "agreement" within the meaning of the Sherman Act; the manufacturer is free to impose the practical sanction of refusing to deal with those who do not follow the suggested prices.⁴¹

The *Colgate* Court distinguished *Dr. Miles* as a case where an agreement clearly existed. Consequently, future litigation had to plot out the lines of permissible manufacturer conduct by judgments about whether such conduct constituted an agreement or not.⁴² When it became apparent that manufacturer conduct falling well short of an agreement in

38. *Id.* at 307.

39. *Id.*

40. *Dr. Miles* was regarded as wholly different because the arrangement in that case "was effected through contracts which undertook to prevent dealers from freely exercising the right to sell." *Id.* at 308.

41. The Court stated:

We cannot . . . wholly disregard the statement that "the retailer . . . could, if he chose, give away his purchase, or sell it at any price he saw fit" We must conclude that . . . the indictment does not charge *Colgate* . . . with selling its products to dealers under agreements which obligated the latter not to resell except at prices fixed by the company.

Id. at 306-07.

42. It has been regretted that so critical a juncture of the law should have been decided by so "unworthy" a case as *Colgate*. See Levi, *The Parke, Davis-Colgate Doctrine: The Ban on Resale Price Maintenance*, 1960 SUP. CT. REV. 258, 285.

any conventional sense nevertheless would threaten the values *Dr. Miles* sought to promote, the Court had to choose whether to abandon the *Dr. Miles* policy against vertical price fixing or to expand the concept of agreement artificially. The Court chose the latter alternative with the result that liability now turns on "an imaginary inference [of agreement], all askew from the normal meaning of [the term]."⁴³

The doctrine developed in distinct stages. The Court first conceded that the necessary agreement need not be express, but could be "implied from a course of dealing or other circumstances."⁴⁴ Then, in *FTC v. Beech-Nut Packing Co.*,⁴⁵ the Court held that an "agreement" may be found although it is not even implicit. Beech-Nut entered into negotiations with dealers seeking assurances from them that they would comply with the manufacturer's wishes. The Court found that such practices "are quite as effectual as agreements express or implied intended to accomplish the same purpose."⁴⁶

The movement away from requiring some actual consensus between the parties continued. Finally, in *United States v. Parke, Davis & Co.*,⁴⁷ the Court so modified the "agreement" element that it now retains none of its original consensual meaning. "Agreement" has become a code word meaning only that the manufacturer has pursued its price preferences with an unacceptable vigor. The *Parke, Davis* Court explained:

[*Colgate* meant] no more than that a simple refusal to sell . . . is permissible under the Sherman Act. In other words, an unlawful combination is not just such as arises from a[n] . . . *agreement*, express or implied; such combination is also organized if the producer secures adherence to his suggested prices by means which go beyond his mere declination to sell to a customer who will not observe his announced policy.⁴⁸

The practical effect of this line of cases is the subject of continuing

43. *Id.* at 294.

44. *United States v. Shrader's Son, Inc.*, 252 U.S. 85, 99 (1919).

45. 257 U.S. 441 (1922).

46. *Id.* at 455.

47. 362 U.S. 29 (1960).

48. *Id.* at 43. The Court was clear about the price paid for this freedom on the part of the manufacturer. The danger that horizontal competition would be affected was conceded: "True, there results the same economic effect as is accomplished by a prohibited combination to suppress price competition if such customer, although induced to do so solely by a manufacturer's announced policy, independently decides to observe specified resale prices." *Id.* at 44. The Court further conceded that manufacturer suggestions may, in fact, induce retailers to use the suggested price by giving them some assurance that they will not be undercut by other retailers. "It must be admitted that a seller's announcement that he will not deal with customers who do not observe his policy may tend to engender confidence in each customer that if he complies his competitors will also." *Id.* at 46.

debate.⁴⁹ Many feel that the immunity *Colgate* conferred on a manufacturer has been wholly eliminated by the judicial willingness to find the requisite "agreement" in virtually any manufacturer conduct. The dissenting justices in *Parke, Davis* were of the view that the majority so limited the *Colgate* doctrine as to "eviscerate" it and "throw the . . . doctrine into discard."⁵⁰ At most, the *Colgate* doctrine is said by the courts to confer only a "limited dispensation" to manufacturer efforts to control resale prices,⁵¹ and to provide only a "narrow channel through which [the manufacturer] may pass," a channel so narrow as to be impassable by any arrangement which is not of "Doric simplicity."⁵²

C. Recent Cases on the *Colgate* Immunity

Although the majority of the commentators suggest that the *Colgate* protection is so thin as to be imaginary and that the law today therefore practically forecloses all forms of vertical price tampering, a number of manufacturers have successfully negotiated the *Colgate* "channel." Even looking at the fractional measure represented by litigated cases, one has the impression that the rumors of *Colgate*'s death have been greatly exaggerated. Although the cases have not produced any intellectually coherent doctrine, a brief review of some recent opinions will illustrate the continuing problem.

A common judicial approach has been to grant *Colgate* immunity when there is no evidence of dealer coercion.⁵³ For example, in *United States v. O. M. Scott & Sons Co.*,⁵⁴ the manufacturer of lawn care products preticketed them,⁵⁵ nationally advertised the retail price, and encouraged dealers to refuse to sell to other dealers who might discount the products. The manufacturer never cut off any dealer even though there was occasionally some dealer price discounting. In a government suit to

49. See, e.g., L. SULLIVAN, *supra* note 4, at 394; Pitofsky & Dam, *Is the Colgate Doctrine Dead?*, 37 ANTITRUST L.J. 772 (1968).

50. 362 U.S. at 57.

51. *Times-Picayune Pub. Co. v. United States*, 345 U.S. 594, 626 (1953).

52. *G. W. Warner & Co. v. Black & Decker Mfg. Co.*, 227 F.2d 787, 790 (2d Cir. 1960).

53. In an early franchise case, the plaintiff, whose franchise was terminated, testified that he alone determined the price, in spite of the manufacturer's transmission of price suggestions, thus negating that the manufacturer conduct was coercive in any way. *Engbrecht v. Dairy Queen Co.*, 203 F. Supp. 714 (D. Kan. 1962). See also *Santa Clara Valley Distrib. Co. v. Pabst Brewing Co.*, 556 F.2d 942 (9th Cir. 1977). In *Santa Clara* witnesses of the plaintiff-dealer testified at length that they were never threatened by the manufacturer, that the manufacturer never forced them to comply with its suggestions as to price, and that they always felt free to charge what they pleased. On that evidence, a verdict was directed for the defendant manufacturer.

54. 303 F. Supp. 141 (D.D.C. 1969).

55. The word "preticketing" refers to imprinting the manufacturer's suggested resale price on the package or the product itself, or on an attached tag.

enjoin Scott, the court held that no dealer was caused "to change his normal manner of doing business,"⁵⁶ and that therefore the injunction would not issue. The court said that to go beyond the limit of *Colgate* protection there "must be such [manufacturer conduct] as to induce an acquiescence in the dealer that is not of his free choice. . . . [There must be] some element of coercion" ⁵⁷

Coercion may be just another way of characterizing the kind of relationship between the manufacturer and the dealer which will be held to be an "agreement" under *Parke, Davis*. The Ninth Circuit, in *Santa Clara Valley Distributing Co. v. Pabst Brewing Co.*,⁵⁸ indicated that without coercion there can be no conspiracy because the notion of conspiracy necessarily includes a "plurality" component. Plaintiff had denied entering into any agreement with the defendant to fix prices, and hence the "plurality" component could be satisfied only by proof of coercion. On its face, of course, this is a bizarre notion of conspiracy but, at least since *Albrecht v. Herald Co.*,⁵⁹ antitrust lawyers have become accustomed to the idea that co-conspirators need not be friends; they can be enemies or even innocent bystanders.⁶⁰

Termination of a conspiracy may also insulate the manufacturer from antitrust liability for cutting off any dealers who were involved in the original conspiracy. In *Dart Drug Corp. v. Parke, Davis & Co.*,⁶¹ a treble damage action growing out of the conspiracy established in *Parke, Davis*, the dealer complained that its role in calling the manufacturer's conduct to the attention of the Justice Department and its role in testifying against Parke, Davis in that litigation were the real reasons Parke, Davis cut it off. The court found, however, that the original conspiracy had terminated with the consent decree in the *Parke, Davis* litigation, and because the plaintiff proved no further conspiratorial behavior after the date of the decree, summary judgment for defendant was affirmed.

The availability of *Colgate* protection may also depend upon whether the manufacturer's attempt to affect resale prices is successful.⁶² *Schnapps Shop, Inc. v. H. W. Wright & Co.*,⁶³ a case involving two

56. 303 F. Supp. at 154.

57. *Id.* at 153.

58. 556 F.2d 942 (9th Cir. 1977). See note 53 *supra*.

59. 390 U.S. 145 (1968).

60. *Id.* at 150 n.6.

61. 344 F.2d 173 (D.C. Cir. 1965).

62. If the degree of success is persuasive to an antitrust court evaluating a suggested price program, another difference between the horizontal and vertical price fixing doctrines appears. In horizontal cases, whether the price fixers have any effect or even the power necessary for potential effect are both, by conventional analysis, irrelevant to the condemnation of the conduct. See L. SULLIVAN, *supra* note 4, at 198.

63. 377 F. Supp. 570 (D. Md. 1973).

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manufacturers, one held to be within the *Colgate* protection and the other not, illustrates the subtlety of this analysis. Universal and Wright sold liquor to the plaintiff, Schnapps. Both manufacturers published suggested list prices, discouraged dealers from price cutting, obtained information that plaintiff sold its product at less than the suggested price, "requested" that Schnapps alter its policies and ultimately refused to sell to it. Schnapps then brought an antitrust action against both suppliers under section 1 of the Sherman Act.

Universal's conduct, said the court, did not violate the antitrust laws because there was no agreement; the court seemed to use the word "agreement" in its consensual or contractual sense. At most, Universal's actions were "preliminaries to solicitation of agreements by retailers to maintain a united advertised-price front."⁶⁴ Alternatively, Universal may have "invited concerted action." But more than solicitations and invitations are needed; "[w]ithout the crucial steps of invitation and acceptance, no conspiracy . . . exists."⁶⁵

Wright, however, was held to have gone beyond the protection of *Colgate*. The court observed that, unlike Universal, Wright had been very successful in controlling retail prices. Of some 4,000 dealers subjected to Wright's entreaties, all but about ten complied with the pricing suggestions. Although the court said that success itself would not prove a conspiracy, the conclusion is almost irresistible that the court found in the widespread compliance with Wright's suggestions the "acceptance" of the supplier's "invitation" needed to establish the conspiracy.

The manufacturer may also prevail because of failures of proof. Given the uncertain nature of the doctrine in this area, the credibility of evidence is critical.⁶⁶ In *Garretts, Inc. v. Farrah Mfg. Co.*,⁶⁷ the plaintiff,

64. *Id.* at 576.

65. *Id.*

66. The quantum of proof required will of course vary with the standard the court applies to determine whether *Colgate* protection is available to the defendant. *Klein v. American Luggage Works, Inc.*, 323 F.2d 787 (3d Cir. 1963), illustrates the difficulty of predicting how freely a court will infer an agreement or conspiracy from sketchy or conflicting evidence. The district court found evidence that the manufacturer informed dealers of the plan to support prices and that the dealers adhered to the plan. The evidence also showed that the manufacturer's product was preticketed, that the manufacturer's salesmen told dealers that compliance with price suggestions was mandatory, and that retailers agreed to this, in part responding to a volume of manufacturer literature and other communications during the negotiation for a sale to the dealers. The district court found the necessary agreement, applying the *Interstate Circuit* formula (*Interstate Circuit v. United States*, 306 U.S. 208 (1939)) to the effect that an actual agreement is not necessary for the offense if concerted action was contemplated and invited and defendant's conduct appeared responsive to the invitation. The court of appeals reversed on the ground that the finding below was unsupported by the record. The record showed only that the manufacturer "advised" the dealers as to its preference, and this was within *Colgate* protection. The court of appeals expressly denied that the *Interstate Circuit* formula could apply on these facts.

67. 412 F. Supp. 656 (D.S.C. 1976).

cut off by the defendant manufacturer for discounting the defendant's product, chose a nonjury trial. His witnesses stated that there were threats by the defendant, contacts between the defendant's salesmen and the plaintiff's employees, and contacts between the defendant and other retailers. The defendant's witnesses stated that after noticing the plaintiff's price cutting behavior, they strictly avoided the plaintiff, said nothing to him, simply stopped calling on him and refused further dealing. Among the defendant's witnesses were other retailers who testified that the defendant never put any pressure on them to maintain retail prices. The district court judge believed the defendant's witness. The judge conceded that the *Colgate* channel was a narrow one; nevertheless, he said, "the credible evidence presented shows that defendant has charted and sailed a course simple enough to negotiate it successfully."⁶⁸

A manufacturer may also navigate the *Colgate* channel by reducing the directness of the price control. In *Engbrecht v. Dairy Queen Co.*,⁶⁹ for example, the manufacturer disseminated information locally and nationally about the price at which one could buy its products in its own retail outlets. The court found this to be within the *Colgate* protection. In *United States v. UniRoyal*⁷⁰ the court refused to hold a manufacturer liable for the sporadic and isolated acts of its salesmen who, contrary to company policy, may have individually crossed the *Colgate* line.

Finally, with doctrine so unclear and the vagaries of proof so great, there is perhaps more room than usual for the play of the fact-finder's own bias. A court is not likely to be generous in evaluating the elements of an antitrust case in favor of a plaintiff appearing to the court as one who, "like many another loser in the competitive endeavor, . . . decided to try the antitrust laws as a means of shifting his loss to someone else."⁷¹

III. THE CASE AGAINST SUGGESTED RESALE PRICES

The foregoing discussion illustrates a number of means by which the *Colgate* channel has been successfully navigated. The result is that despite the per se rule against price fixing, vertical price tampering is permitted in broad ranges when it takes the form of manufacturer suggestions enforced by refusals to deal. Thus, to the extent that protection for

68. *Id.* at 665. The judge's preference for defendant's witnesses was based in part on the fact that in the eyes of the judge they were not interested, while plaintiff's witnesses were. One wonders, however, how objective plaintiff's competitors were, when called by defendant to establish that the defendant had lawfully eliminated one of their most troublesome competitors.

69. 203 F. Supp. 714 (D. Kan. 1962).

70. 300 F. Supp. 84 (S.D.N.Y. 1969).

71. *C. O. Hanson v. Shell Oil Co.*, 541 F.2d. 1352, 1355 (9th Cir. 1976).

such conduct is available under the *Colgate* doctrine, the accepted antitrust policy against vertical price fixing is frustrated. The remainder of this article argues that the *Colgate* rule should be modified at least to the point of making suggested prices presumptively illegal. Fuller enforcement of the ban on vertical price fixing would generate doctrinal clarity and predictability and is in the interest of a general strengthening of competition.

A. *The Value of Doctrinal Clarity*

The cases illustrate that whether a manufacturer's conduct has crossed the line of *Colgate* immunity often depends upon a court characterizing otherwise unilateral conduct as an agreement. The doctrine is obscure because the notion of agreement has taken on an artificial meaning. Although a manufacturer price suggestion, followed by acquiescence on the part of the dealer, could be considered an agreement in a conventional sense,⁷² the doctrine requires that that notion be rejected while allowing the courts to go on and find the necessary agreement in conduct wholly without consensual content. As the preceding discussion illustrates, courts can find an agreement when the manufacturer listens to complaints from other retailers about plaintiff's price cutting,⁷³ urges the price-cutting dealer to hold the line on prices,⁷⁴ or explains his pricing preferences in repeated or enthusiastic terms.⁷⁵ This conduct, of course, adds nothing consensual to the transaction. The result is an unwelcome doctrinal obscurity. The language is further strained when the victim of the conspiracy is held to be a co-conspirator, or innocent third parties are said unknowingly to make conspiratorial what would otherwise be unilateral.⁷⁶

Linguistic purity is not the ultimate objective of a legal system, of course; definitional conventions should not be allowed to impede the solution of problems. But straying from convention does carry some risk of artificiality and imprecision in doctrine, which in turn may impede principled decision making and reduce predictability. Altering the normal consensual meaning of "contract, combination, or conspiracy," has for example, caused liability in this area to turn on such matters as the vigor

72. "[I]t should be . . . clear . . . that a policy of refusing to deal with price cutters is no more nor less than an invitation to agree on resale price which, if it produces the desired acquiescence . . . , results in . . . agreements." Turner, *supra* note 19, at 689.

73. See *Schnapps Shop, Inc. v. H. W. Wright & Co.*, 377 F. Supp. 570 (D. Md. 1973).

74. See *United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960).

75. See *Coors v. FTC*, 497 F.2d 1178 (10th Cir. 1974).

76. See, e.g., *Albrecht v. Herald Co.*, 390 U.S. 145 (1968).

with which a manufacturer happens to phrase his suggestions, the careless remark of a visiting salesman, or the degree to which dealers find it in their interest to go along with manufacturer suggestions. The resulting area of proscribed conduct is not explicable by reference to any of the understood purposes of the antitrust laws, and labeling the conduct an agreement does not remedy this deficiency. If the antitrust laws are to discourage coercion, vigor, and carelessness the issue should be addressed head-on, not decided by the shape of an incidental remnant of the *Colgate* doctrine. Failure to deal with the problem directly has produced doctrine which inexactly implements the purposes of the antitrust laws, contorts the statutory language, and fails to identify the area of proscribed conduct intelligibly.

Predicting liability in this area is now extremely difficult. The counseling which appears in print is appropriately cautious in suggesting that manufacturers are unable to do much to establish the retail prices of their products.⁷⁷ The practice of suggesting prices continues, however. It may be that actual counseling is carrying a different message or that the manufacturers themselves find enough ambiguity in the doctrine and enough uncertainty in the cases to make suggesting prices appear to be worth the gamble. Whatever the case, a more predictive doctrine would facilitate rational counseling.

Finally, current vertical price-fixing doctrine violates the ancient and sensible maxim that courts should not permit the parties to do indirectly what the law forbids doing directly. *Dr. Miles* prohibits the vertical fixing of resale prices, but *Colgate* permits the manufacturer to suggest a price and to punish the dealer who will not comply with it by refusing to sell to that dealer. If the *Dr. Miles* policy against vertical price fixing is sound, and most agree that it is,⁷⁸ circumventing that policy by indirect *Colgate*-approved conduct should not be allowed. It is true that the line of cases including *Parke, Davis*, with their expanded notion of agreement, curtails somewhat this circumvention of the *Dr. Miles* policy. As has been indicated, however, the drawbacks of this indirect solution leave the antitrust doctrine unsound, analytically confused, and unpredictable. The *Colgate* problem should be squarely faced and the doctrine explicitly revised unless it has significant practical justifications or unless suitable alternatives cannot be fashioned.

77. See, e.g., C. HILLS, ANTITRUST ADVISER § 232 (2d ed. 1978); E. ROCKEFELLER, ANTITRUST QUESTIONS AND ANSWERS 110 (1974).

78. It is not strictly accurate to say that all agree with the *Dr. Miles* proscription of vertical price fixing. See R. BORK, ANTITRUST PARADOX 288-91 (1978). But the weight of the commentary and the express statements of the Court indicate acceptance of the principle. See L. SULLIVAN, *supra* note 4, at 377.

B. The Competitive Effects of Suggested Resale Prices

Two justifications for the different practical treatment of vertical and horizontal price fixing usually are advanced. First, there are said to be benefits of vertical price restrictions which do not exist in the case of horizontal restrictions and which therefore warrant some judicial generosity. Second, the potential harms of price restraints between vertically related parties are said to be less than the harms associated with horizontal price restraints.

1. Benefits

The existence and extent of benefits flowing from vertical price restraints generally are the subject of considerable debate. In *Dr. Miles*, Justice Hughes doubted that there was significant manufacturer interest in formal resale price fixing: "[T]he advantage of established retail prices primarily concerns the dealers. The enlarged profits which would result from adherence to the established rates would go to them and not to the [manufacturer]."⁷⁹ A substantial controversy has broken out since that time over whether manufacturers have significant and legitimate interests in controlling resale prices. The literature contains several lists of asserted advantages and there is no need to detail them here.⁸⁰

A central theme of the literature is the recognition that the manufacturer must pay to have its product distributed and marketed and if it chooses to have those functions performed by persons outside the firm it must pay what is necessary to induce the appropriate kind and degree of marketing efforts. When, for example, successful promotion and marketing of a product requires such things as demonstrations, advertising, or warranty service, someone must be induced to perform those services. When the manufacturer fixes the retail price it frees the dealer from intra-brand competition, presumably permitting the dealer to charge a somewhat higher price for the product. The extra returns compensate the dealer for additional services performed. It is said that since fixed resale prices make intrabrand price competition impossible, dealers channel their competitive energies into service competition, thus guaranteeing the

79. 220 U.S. at 407.

80. See, e.g., the tabulations of manufacturer benefits in R. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* 147-51 (1976); F. SHERER, *INDUSTRIAL MARKET STRUCTURE* 513-15 (1970); L. SULLIVAN, *supra* note 4, at 380; Bork, *The Rule of Reason and the Per Se Concept*, 75 YALE L.J. 373, 453 (1966); Louis, *Vertical Distributional Restraints Under Schwinn and Sylvania: An Argument for the Continuing Use of a Partial Per Se Approach*, 75 MICH. L. REV. 275, 296-306 (1976); Tester, *supra* note 2; Note, *The Legal and Economic Status of Vertical Restraints*, 23 VILL. L. REV. 547, 561-69 (1978).

manufacturer needed marketing functions. Viewed from a slightly different angle, some manufacturer control of resale prices is said to be needed because of the "free rider" problem: the dealer cannot be expected to offer elaborate and expensive demonstrations of a product if the customer—having made his selection by reason of the dealer's demonstration—actually buys the product from a discount house which is able to undercut the dealer's price because it does not bear the expense of demonstrating the product.

Another manufacturer justification for control of resale prices is said to lie in capturing scale economies in advertising, for example, stabilizing the retail price of the product so that a manufacturer can take advantage of national advertising programs.⁸¹

It is sometimes said that the elimination of intrabrand competition facilitates the promotion of products which are new or have small market shares, leading to increased interbrand competition. It is also suggested that a manufacturer may be confronted with a cartel at the retail level which is pricing its products too high for maximum manufacturer profit. By having control over resale price, a manufacturer could impose a *maximum* retail price and thus protect the consumer from price gouging on the part of local cartels or monopolies.⁸²

Other motives or explanations for resale price maintenance are offered but do not appear to generate benefits that would be weighted favorably from an antitrust standpoint. Some of these are essentially neutral from the antitrust perspective, such as the notion that manufacturer control of resale price aids the manufacturer in protecting its brand image by reducing the probability of loss-leader pricing.⁸³ Still other suggested motives are actually antithetical to antitrust concerns, such as the justification that the manufacturer, more than the retailer, knows the real shape of the consumer demand curve or the real composition of dealers' costs and therefore is better able to establish the appropriate price. Although superficially appealing, in some settings general manufacturer control of retail prices is likely to undercut important competitive values and to produce rigidity and unresponsiveness in retail pricing.⁸⁴ The same may be said for the suggestion that control of resale price gives the manufacturer control over the entire distribution system, including the important choices of who, where and how its product will be marketed.⁸⁵ It is said that

81. See Bork, *supra* note 80, at 460.

82. *Id.* at 464.

83. P. AREEDA, *ANTITRUST ANALYSIS* 501-02 (2d ed. 1974).

84. L. SULLIVAN, *supra* note 4, at 381-82, 388.

85. See L. Stern, *Approaches to Achieving Retail Price Stability*, in *CONCEPTS FOR MODERN MARKETING* 177 (R. Day ed. 1968).

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manufacturers should also be concerned about supporting resale prices because price competition, if allowed to break out of the retail level, may well back up into the manufacturer level as retailers put pressures on manufacturers to cut wholesale prices.⁸⁶ That, of course, would be precisely the hoped-for outcome of significant competitive pressure at the retail level. Finally, there is little doubt that manufacturer control of resale prices can facilitate cartels at the manufacturer levels, an outcome which would run directly counter to a central policy of the antitrust laws.⁸⁷ This may occur in a variety of ways, as for example, when the existence of uniform resale prices makes manufacturer "cheating" more visible to the other members of the cartel, or when the existence of a fixed resale price removes the motivation for manufacturer price competition.⁸⁸

Most of the asserted justifications for manufacturer control of resale prices draw strength from the supposition that the interest of the manufacturer in retail prices is nearer to that of the consumer and is usually contrary to the interest of the retail dealer. When price-affecting conduct takes place between horizontal competitors, there is no reason to believe much is involved other than the suppression of competition, which carries a heavy cost in terms of the consumer interest. Horizontal competitors will generally prefer higher rather than lower dealer profits. But at any fixed manufacturer selling price, it would seem to be in the interest of the manufacturer that the dealer's markup be as low as possible in order that the retail price be minimized. This insures that the maximum number of units will be sold to consumers, and the greater the number sold, the greater will be the manufacturer's revenues. Because minimizing dealer profits is in the interest of the consumer as well as the manufacturer, it is argued that permitting the manufacturer to impose some price-affecting restraints on dealers does not significantly threaten consumer interests.⁸⁹

Whether vertical restrictions of these kinds are always so innocent has been questioned.⁹⁰ The model described above may have a real world counterpart when the manufacturer is a monopolist. When the manufacturer itself faces competition at the manufacturer level, however, there may be incentive to increase dealer profits in the hope of inducing dealer

86. *Id.* at 192.

87. See FTC REPORT ON RESALE PRICE MAINTENANCE lxii (1945); Tester, *supra* note 2, at 96-104; R. BORK, *supra* note 78, at 293 (stating view that the problem is not a substantial one); F. SHERER, *supra* note 80, at 512-15.

88. See Tester, *supra* note 2, at 96-99.

89. See L. SULLIVAN, *supra* note 4, at 380.

90. *Id.* at 411-21.

conduct aimed at creating consumer preferences for the manufacturer's product.⁹¹ If additional dealer promotion induced by higher markups in fact increases the number of sales, the manufacturer and the dealer may both gain; it is not obvious that the consumer is benefited.⁹²

Moreover, it should be obvious that one cannot justify a manufacturer-imposed *minimum* price on any theory that the manufacturer is more interested than the dealer in the lowest possible price. Wherever the manufacturer feels the need to prevent the dealer from lowering the retail price, the consumer is presumably better off with the dealer's price preference.

Another difficulty with the general justification for vertical restraints is that it tends to overlook the effect of such restraints on the manufacturer's market power. Vertical restraints are principally aimed at increasing market power of the products involved through product differentiation. It seems likely that the objective of most dealer services of the promotional variety is the differentiation of the manufacturer's product from that of its competitors. To the extent this effort succeeds, competing products no longer appear to the consumer as effective substitutes and interbrand competition becomes less effective: the product's price increases may be made without fear of significant loss of trade.

There is considerable incentive . . . for firms to differentiate their products from those of their rivals precisely for the purpose of promoting low consumer substitutability, thereby insulating themselves from the effects of price competition.

[In consequence, the] manufacturer and the dealer are both likely to benefit—at the consumer's expense—from the high dealer markups required for product differentiation

. . . .

. . . In the end, vertical restrictions not only will eliminate intrabrand competition but also, through their effect on product differentiation, will serve to restrict price competition among the products of different firms.⁹³

When one turns from the general justifications for vertical price restraints to inquire into the likely effects of the particular form of price restriction under review here—*suggested* resale prices—the benefits analysis grows even more attenuated. As has been indicated above,⁹⁴ the *Sylvania* opinion has relaxed the rigid rule regarding nonprice vertical restraints, in part because of a perception that such restraints may involve

91. Comanor, *supra* note 5, at 1425.

92. *Id.* at 1426.

93. *Id.* at 1423, 1426–27.

94. See text accompanying notes 9–12 *supra*.

benefits to competition. Most would agree that any benefits derived from vertical nonprice restraints are primarily due to the manufacturer's ability to insist on the restraint. That is, it is the manufacturer's ability to *force* dealers to stay within certain territorial limits or to sell only to certain customer classes which assures other dealers of freedom from intrabrand competition. In turn, that freedom is said to induce the additional promotional activity which benefits the manufacturer.⁹⁵ A system of "voluntary" territorial assignments, or "suggested" customer limitations, however, will not ensure any benefit to the manufacturer. For this reason, few if any manufacturer benefits could ever be traced to a system of "suggested" list prices. Suggested prices do not guarantee dealer freedom from intrabrand competition. That freedom arises only when other retailers decide that it is in their interest to comply with the price suggestion. Manufacturer benefits bought at such a cost to competition are, it is argued below, far too expensive. In short, it is very difficult to distinguish this situation from price tampering in the horizontal context when the obvious harms to the consumer outweigh any conceivable benefits to competition.

2. Harms

If the claimed benefits of suggested prices are speculative or costly, any justification of them must show that the harms involved are minimal. In addition to the potential harms of vertical restraints generally, as reviewed above, and to the special harms at the manufacturer level which have been suggested, the most obvious competitive costs of the practice of suggesting prices are paid in terms of reduced competition at the retail level. As was clear to Justice Hughes as early as 1911,⁹⁶ the practice of resale price maintenance can substantially eliminate price competition among the retail sellers of the product in question. This conclusion is challenged by those who feel that the consumer is not harmed by the elimination of intrabrand competition if there is sufficient interbrand competition present in the market. For example, the manufacturer of XYZ television sets, desiring to encourage dealers to provide more comfortable showrooms, more elaborate demonstrations, or improved warranty service, may impose price restraints on its dealers; all XYZ television sets of any given model will henceforth sell at the same price. The

95. The conventional assertions that vertical restrictions have the effect of producing a level of dealer services desired by the manufacturers have been criticized. *E.g.*, Comanor, *supra* note 5, at 1432-33; Comment, *The Legal and Economic Status of Vertical Restrictions*, 23 VILL. L. REV. 547, 562 (1978).

96. See note 26 and accompanying text *supra*.

consumer is obviously deprived of price competition among XYZ dealers, but, it is argued, the consumer is not hurt by this arrangement if there are substitute brands available because that availability means that XYZ prices cannot be much above the competitive level for television sets, including the cost of the additional services calculated at their value to the consumer. If XYZ's price were higher, by definition XYZ would lose trade to competing brands. The price restraint, then, far from being harmful to the consumer, instead makes available to him additional services should he desire them.

This line of reasoning is unpersuasive for three reasons. First, no one believes the argument justifies comparable horizontal arrangements. Second, interbrand competition is not an adequate substitute for intrabrand competition. And, third, arrangements eliminating intrabrand competition too likely facilitate the operation of a dealer cartel or, at least, facilitate cartelization if it has not already occurred.

If enhancing interbrand competition were an adequate justification for eliminating intrabrand competition, horizontal arrangements for this purpose should be allowed. No one, however, has argued that horizontally related dealers of a single brand should be allowed to combine to set prices for that brand on the theory that only intrabrand competition is affected.⁹⁷ If all the Plymouth dealers in town wanted to agree on the price of the various models of that automobile, the arrangement would be condemned absolutely. The dealers could not justify their conduct by saying that so long as Chevrolets are available to the consumer there will be no harm in permitting Plymouth dealers to agree on Plymouth prices.⁹⁸

Even conceding, for the sake of argument, the validity of the suggestion that consumer welfare is more protected when the manufacturer sets prices than when prices are set by horizontal competitors,⁹⁹ the example of the Plymouth dealer cartel indicates the limits of the protection by illustrating the second, more fundamental failure of the argument that the consumer is adequately protected by the existence of interbrand competition. Interbrand competition is not an adequate substitute for the intrabrand competition eliminated. Manufacturers will not attempt to fix resale prices unless there is some market power in the brand whose price is being fixed. If there is no market power in the brand, that is, if there are perfect substitutes in the market, the elimination of intrabrand competition by controlling resale prices would be pointless. Any effort

97. See *United States v. Topco Assocs., Inc.*, 405 U.S. 596 (1972); *United States v. Sealy, Inc.*, 388 U.S. 350 (1967); *Plymouth Dealers' Ass'n v. United States*, 279 F.2d 128 (9th Cir. 1960).

98. See *Plymouth Dealers' Ass'n v. United States*, 279 F.2d 128 (9th Cir. 1960).

99. See note 89 and accompanying text *supra*.

by the dealer to raise its price above that of other brands would suffer a loss of business to those brands.¹⁰⁰ Accordingly, whenever manufacturers attempt to control resale prices, one can assume that there is sufficient market power in the brand to support trade at the higher prices. And when market power exists for a given brand, intrabrand competition is important. In short, the manufacturer's justification for vertical restraints assumes the existence of perfectly substitutable products, which is most unlikely in the typical setting in which vertical restraints are appealing.

Market power is often generated by the manufacturers themselves. Auto makers, for example, spend vast sums to differentiate their products. The result is that Chevrolets and Plymouths are not fully substitutable. The consumer who has become persuaded, perhaps as a result of manufacturer advertising, that Plymouth is the only brand to buy should have the benefit of competition among Plymouth dealers. A manufacturer claim of the right to reduce competition among its dealers because the consumer is not harmed so long as differentiated products are available has a hollow and unpersuasive ring.¹⁰¹

The third problem with vertical arrangements to set prices is that they are very likely to be integral to the operation or formation of a dealer cartel. It is said that vertical price restraints are valuable because they induce dealers to finance additional promotional and other point-of-sale services which are important to the manufacturer's marketing strategy. This inducement depends upon two circumstances.¹⁰² First, it is necessary that the price suggested by the manufacturer is above that which would be set by the forces of the competitive market. If the manufacturer set a price below the market, of course, no dealer would comply. Second, even though the price suggested is attractive, no dealer will willingly adopt it unless he expects his competitors also to conform. The expectation of general compliance among dealers is thus the second necessary condition. In a form of the familiar "recognized interdependence" phenomenon,¹⁰³ dealers may recognize that they are better off if all conform to the

100. For a technical explanation of this notion, see E. DOUGLAS, *ECONOMICS OF MARKETING* 208 (1975).

101. "[Intrabrand competition] may often be vital to the consumer, especially in industries where products are so highly differentiated that a particular brand often has a market of its own." R. Favretto, *Vertical Restraints and Other Current Distribution Issues in the Wake of Sylvania 9* (Remarks at Southwestern Legal Foundation Symposium on Antitrust Law in Dallas, Texas, May 12, 1978). See also F. SHERER, *supra* note 80, at 515; L. SULLIVAN, *supra* note 4, at 379; Zimmerman, *Distribution Restrictions After Sealy and Schwinn*, 12 ANTITRUST BULL. 1181, 1185 (1967).

102. See Comment, *Refusal to Sell: A Means of Achieving Resale Price Maintenance in Non-Fair-Trade States*, 36 TEX. L. REV. 799 (1958).

103. See F. SHERER, *supra* note 80, ch. 5; L. SULLIVAN, *supra* note 4, at 331-43; Turner, *supra* note 19.

manufacturer's supracompetitive price suggestions. The pricing conduct thus rests on an explicit or tacit understanding among horizontal competitors which, if directly achieved, would be condemned.¹⁰⁴

The cartelization process is greatly facilitated by manufacturer suggested price systems. There is little doubt that whenever some retailer interest in price stability is present, any kind of target price will facilitate the achievement of that stability. "Focal point" pricing, "bench mark" pricing, price signalling, or other facilitating devices can have significant effects on retail price uniformity.¹⁰⁵ If such subtle measures can produce unnecessarily stable retail prices, discrete and specific price information printed directly on a label or package or appearing in an advertisement certainly can have the same effect. When overt communication would be legally risky, suggested prices and preticketing would be an ideal solution for retailers looking for an effective means of "coordinating" their actions for their mutual benefit.¹⁰⁶

A manufacturer-generated price target may have the identical effect of one generated by a retailer association and retailer tampering with price is everywhere condemned. Circulation among retailers of pricing "guides" was characterized as price fixing and held to violate the Sherman Act in *United States v. Nationwide Trailer Rental System, Inc.*¹⁰⁷ Distribution of a dealers' association "suggested price" was held unlawful in *Plymouth Dealers' Association v. United States*¹⁰⁸ even though dealers were not committed to and many did not follow the suggested prices. Competitors cannot safely set a time at which prices are to be individually set,¹⁰⁹ establish a functional discount rate¹¹⁰ or an advertising policy,¹¹¹ or determine jointly the composition of the industry's product,¹¹² even though none of these practices can be said to have any necessary effect on actual prices. To make this sort of conduct a per se violation it is enough, in the classic formulation in *United States v. So-*

104. See note 26 *supra*.

105. See Blechman, *Conscious Parallelism, Signalling and Facilitating Devices: The Problem of Tacit Collusion Under the Antitrust Laws*, 24 N.Y.L. Rev. 881, 901-03 (1979); Kuhlman, *Price Fixing, Nonprice Competition and 'Focal Point' Pricing: A Rose by Any Other Name*, 10 ANTITRUST L. & ECON. REV. 75 (1978). The Federal Trade Commission has recently commenced a proceeding against manufacturers of gasoline additives in part based on price signalling. TRADE REG. REPORTS (CCH) No. 388, at 1 (June 5, 1979).

106. See Kuhlman, *supra* note 105.

107. 156 F. Supp. 800 (D. Kan.), *aff'd per curiam*, 355 U.S. 10 (1957).

108. 279 F.2d 128 (9th Cir. 1960).

109. *United States v. Jantzen Inc.*, [1966] Trade Cas. (CCH) 83, 110 (D. Ore.)

110. *United States v. United Liquors Corp.*, 149 F. Supp. 609 (W.D. Tenn. 1956), *aff'd*, 352 U.S. 991 (1957).

111. *United States v. Gasoline Retailers Ass'n*, 285 F.2d 688 (7th Cir. 1961).

112. *Nat'l Macaroni Mfr. Ass'n v. FTC*, 345 F.2d 421 (7th Cir. 1965).

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cony Vacuum Oil Co.,¹¹³ that the conduct has the purpose or effect of “raising, depressing, fixing, pegging or stabilizing” prices.

In addition to the harmful *effects* on horizontal competition, the historical record supports the idea that there may be anticompetitive *purposes* as well. The most developed literature concerning the purposes behind manufacturer control of retail prices is in the fair trade area. The history of that area reveals that resale price maintenance under the fair trade laws was virtually everywhere retailer inspired.¹¹⁴ After a review of the history, Professor Bowman says:

The foregoing examples suggest that resale price maintenance is a method used by organized dealers to force unwilling manufacturers to work for them to protect dealer profit margins. . . .

The pressure and the moral force of the [retailer] association is responsible more than any other single factor for whatever price maintenance we have¹¹⁵

Large retailer organizations mounted massive lobbying efforts which secured the enactment of fair trade laws in many states, and manufacturers who fought this movement ultimately had to reckon with retailer retaliation.¹¹⁶

The history of the fair trade laws also makes it relatively clear that once those laws were adopted, the manufacturing component of the marketing system was enlisted as an enforcement agency to further programs in the interest of retail dealers. In reviewing the variety of devices by which retail associations could police their own cartels, Professor Hollander says a common finding is “pressure or persuasion on an outside agency to enforce the group program. This is why so many retailer price arrangements become vertical plans, with the suppliers placed in the role of enforcement agency.”¹¹⁷

In summary, the retail level effects of suggested prices are serious. Their widespread use signals significant market power in the brand involved as well as a common perception among horizontal competitors that they will benefit by jointly following the manufacturer’s suggestions. The sort of parallel behavior which results from perceived interde-

113. 310 U.S. 150, 223 (1940).

114. S. HOLLANDER, RESTRAINTS UPON RETAIL COMPETITION 48–70 (1965); R. LYNN, PRICE POLICIES AND MARKETING MANAGEMENT 271 (1967); L. SULLIVAN, *supra* note 4, at 383; Bowman, *The Prerequisites and Effects of Resale Price Maintenance*, 22 CHI. L. REV. 825, 849 (1955).

115. Bowman, *supra* note 114, at 830–31 (quoting FTC, REPORT ON RESELL PRICE MAINTENANCE (1945)).

116. An example of retailer retaliation against a reluctant manufacturer is given in R. LYNN, *supra* note 114, at 271.

117. S. HOLLANDER, *supra* note 114, at 70.

pendence among horizontal competitors has not yet been effectively condemned by the antitrust laws because of the difficulty of devising an effective remedy.¹¹⁸ In the vertical setting, however, this problem does not exist; manufacturer price suggestions can simply be prohibited.

C. *Achieving Vertical "Benefits" at Lower Competitive Cost*

An analysis of the benefits of suggested prices indicates that there are seldom significant benefits to competition that cannot be achieved with less restrictive alternatives. For example, if a manufacturer believes that some national advertising is important to promote its product and that the ads must carry some price information, he can refer to the price generally¹¹⁹ or to a maximum price.¹²⁰ This still gives the dealers a target, yet it is not so clearly a minimum target; the Department of Justice has indicated that the competitive harms may be less than those of suggested prices.¹²¹

The manufacturer who believes that its product is best presented at a specific price, and thus to a specific market, may be able to respond to the discounting problem by developing different product lines for different markets. The makers of Samsonite luggage, for example, market one line through full price outlets and a second line through discounters.¹²² The manufacturer who feels that consumer goodwill is maximized by careful point-of-sale explanation of the uses of the product may achieve some of the same benefits by improving labeling and product literature.¹²³ Another technique is for the manufacturer to pay the dealer directly for point-of-sales services. With some product lines, for example, dealers willing to provide certain services such as promotion and advertising may be paid directly for the service.¹²⁴

Sometimes the product and the service can be priced separately so as to minimize the free-rider problem. If separate pricing is feasible, and if consumers really desire and are willing to pay for a particular service, independent parties may arise to provide it.¹²⁵ It is worth noting that separate pricing of the service produces additional benefits in consumer

118. See Turner, *supra* note 19.

119. E.g., "About \$40."

120. E.g., "Less than \$40."

121. R. Favretto, *supra* note 101, at 23-24.

122. BUSINESS WEEK, Feb. 27, 1965, at 98.

123. See *United States v. O.M. Scott & Sons Co.*, 303 F. Supp. 141 (D.D.C. 1969); text accompanying notes 54-57 *supra*.

124. Comment, *supra* note 95, at 563.

125. Comanor, *supra* note 5, at 1433.

choice: the consumer can better decide which product he wants—the phonograph at a low price without credit terms or warranty service, or the same machine at a higher price with these dealer services.

[A] joint supply arrangement means that consumers are compelled to purchase the entire package; the purchase of dealer services is tied to the purchase of the manufactured product. To the extent that the amounts consumed differ from those which would be chosen in separate markets, resources are misallocated This result seems especially apparent in the case of advertising, for consumers might purchase very little indeed of this “service” were it provided separately.¹²⁶

The manufacturer who is concerned that its product will not be presented well unless certain quality control standards are met, such as the appearance of the showroom or the quality of unpacking and “setting up” functions, may choose to sell only through franchised dealers whose contracts contain minimum quality control requirements.¹²⁷

None of these alternatives is, of course, costless. Because these costs may be passed on to the consumer, it is fair to ask whether the consumer will receive a net benefit from the adoption of a less restrictive alternative. The answer cannot be found with any certainty given the state of our knowledge. According to the view presented in this article there are significant consumer costs in the existing use of suggested prices. Perhaps it would be sensible to require persons imposing those costs to establish that the costs of less restrictive means would be greater.

D. *Other Arguments in Favor of Retaining Colgate*

Indirect benefits are sometimes said to flow from the *Colgate* rule. As indicated earlier,¹²⁸ the *Colgate* Court stated as one of its central propositions that, absent any intent to achieve an anticompetitive outcome, a trader must be free to deal with such customers as he chooses. As part of that freedom, it is said, a manufacturer should retain the right to refuse to deal with price cutters if it does not wish its product marketed in that fashion. The *Colgate* rule protects that freedom by immunizing the manufacturer from antitrust liability for such a refusal to deal. It is feared that overruling *Colgate* will result in forcing a manufacturer to sell to dealers of whose marketing practices it does not approve.¹²⁹

126. *Id.* at 1430.

127. Louis, *supra* note 10, at 303.

128. See note 38 and accompanying text *supra*.

129. See Levi, *supra* note 42, at 284–326.

A variation of this contention is the suggestion that the *Colgate* rule has a useful role in minimizing the use of antitrust litigation as a competitive weapon. Without *Colgate* protection, it is said, a manufacturer who chooses to cut off a dealer for even the purest of motives may be subjected to treble damage liability by a disappointed dealer who can persuade a jury that the cutoff was part of a vertical price-fixing effort. More likely, the threat of such litigation, because it is time-consuming and expensive to defend, may encourage a manufacturer to continue selling to a dealer it no longer wishes to serve. *Colgate* thus tends to protect manufacturers from harassment by disappointed dealers.¹³⁰

There are several responses to these concerns. First, in *Colgate* the Court expressly condemned vertical restraints which had the purpose or intent of producing anti-competitive results. What we now know about the real horizontal and vertical relationships involved makes it appear that virtually all uses of suggested prices have both the purpose and the effect of damaging competition. Thus, the *Colgate* rule according to its own terms can be said to be inapplicable to suggested prices.

Second, it is not unthinkable to impose a duty to deal with all buyers who meet some threshold of responsibility. Other countries have recognized such duties and there is no overpowering evidence that consumer welfare has suffered.¹³¹ There are many occasions in our law when a dealer is obliged to accept customers with whom it might rather not deal. Such occasions are justified whenever society judges total dealer freedom too costly in terms of other more important values.¹³² That would seem accurately to describe the situation here. The dealer freedom protected by *Colgate* costs us a great deal, for its use in the present setting is principally to facilitate horizontal price fixing. The immunity seems plainly too costly to society.

No one should be anxious to impose on private industry a public utility type "duty to serve" or to subject manufacturers to continued harassment by dealers. But we must recognize the competitive harms that may be masked by an unlimited privilege to refuse dealing; we must identify the limits of that privilege which are required to secure the important values of free competitive markets.

130. P. AREEDA, ANTITRUST ANALYSIS 560 (2d ed. 1974).

131. See, e.g., M. HANDLER, H. BLAKE, R. PITOFKY & H. GOLDSCHMID, TRADE REGULATION 611-12 (1975); F. SHERER, *supra* note 80, at 515-16. One distinguished commentator has even suggested that the vaunted right to sell is an American distortion of the common-law right to buy, which is the more important privilege if freely competitive markets are the goal. See V. MUND, THE RIGHT TO BUY—AND ITS DENIAL TO SMALL BUSINESS, S. DOC. NO. 32, 85th Cong., 1st Sess. (1957).

132. Legislative enforcement of civil rights is an obvious example. See J. NOWAK, R. ROTUNDA & J. YOUNG, CONSTITUTIONAL LAW 688-708 (1978).

The danger of the antitrust laws being used as a competitive weapon must also be tolerated in light of the alternative dangers to competition. Of course, one should create doctrine to minimize such misuses of the system whenever possible. It has been suggested, for example, that some of the potential for abuse could be eliminated by requiring a plaintiff to show something more than an isolated instance of manufacturer price tampering before he could get by a defendant's motion to dismiss.¹³³ No doubt, a careful statement of the rule would minimize risk. Beyond that, there are many situations in which exposure to some risk is necessary if the system's underlying objectives are to be met. Indeed, it appears that in the law of antitrust there is often a risk of misuse of the legal process. As Mr. Justice Brandeis has observed in a broader connection, "[l]awsuits . . . often prove to have been groundless; but no way has been discovered of relieving a defendant from the necessity of a trial to establish the fact."¹³⁴

Finally, the matter of remedy must be addressed. Although the dangers presented by suggested prices in part depend on the sort of "tacit collusion" or consciously parallel conduct that is often thought to be beyond the practical reach of a judicial decree,¹³⁵ in its present embodiment the collusion presents no special problems of remedy. The collusion here flows from an objective act—that of suggesting a resale price. A decree forbidding that conduct will effectively eliminate the collusion.

IV. CONCLUSION

Dealers either follow suggested resale prices or they do not. When they do not, no one benefits; the only effect is to create the illusion that the dealer price is something of a discount—a form of consumer fraud the Federal Trade Commission has sought to eliminate.¹³⁶

When dealers do follow manufacturer price suggestions, there are only three reasons to explain the conduct. First, dealers may follow because of manufacturer coercion. Second, dealers may follow the suggestions because it is more convenient for them than computing their own cost data

133. Turner, *supra* note 19, at 690.

134. Myers v. Bethlehem Shipbuilding Corp., 303 U.S. 41, 51–52 (1938).

135. A careful statement of this proposition is found in Turner, *supra* note 19, at 669. Criticism of the notion may be found in R. POSNER, *supra* note 80, at 74, and L. SULLIVAN, *supra* note 4, at 363.

136. See FTC Guides Against Deceptive Pricing, 16 C.F.R. §§ 233.1–.5 (1978). See especially section 233.3, entitled "Advertising retail prices which have been established or suggested by manufacturers."

or making their own estimates of consumer demand. Third, dealers may act as part of a dealer cartel, at least in the de facto sense. None of these reasons promises significant consumer benefits. All of them imply significant harm.

The only explanation for the continued existence of the *Colgate* rule seems to be the absence of parties for whom litigation would be rewarding. If the use of suggested prices is in the interest of the retail dealers and if the manufacturer desires their goodwill, the only people hurt by the existence of the prices are consumers who will not be likely to have a significant enough stake to generate enthusiasm for expensive litigation.¹³⁷ It is relatively clear, too, that the suggested list price problem appears to have a low spot on the enforcement priority scale of public agencies.¹³⁸ The *Colgate* rule does not persist, therefore, because of any advantages or benefits it provides. Rather, it seems to stand only because of the absence of an effective challenge. It is time to end the reign of *Colgate* either by judicial action or administrative decree.

In many cases the Federal Trade Commission has forbidden the use of suggested retail prices when a manufacturer has been thought to be engaged in vertical price fixing.¹³⁹ It would not be such a great step to adopt a rule prohibiting the use of suggested prices generally. It may be that there are situations in which special justifications exist for vertical price suggestions, as when significant consumer benefits are demonstrable, or when the costs of less restrictive alternatives are clearly prohibitive. Further, some freedom from intrabrand competition might result in stronger interbrand competition when new products or infant dealer systems are present.¹⁴⁰ To provide for such situations, it would be sufficient to establish only the presumptive illegality of the suggested price. The manufacturer with a special justification would then have the option of coming forward with his proof.

The legal doctrine required need not be complex or subtle. There is quite enough in the most "unilateral" use of suggested prices to satisfy the requirements of section 1 of the Sherman Act¹⁴¹ or its Federal Trade

137. L. SULLIVAN, *supra* note 4, at 399.

138. *Id.*

139. See, e.g., Pendleton Woolen Mills, Inc., 3 TRADE REG. REP. (CCH) ¶ 21,571 (July 31, 1979) (consent order); Medalist Industries, Inc., [1973-1976 Transfer Binder] TRADE REG. REP. (CCH) ¶ 21,098 (1976) (consent order); Cubco, Inc., *id.* ¶ 20,823 (1975) (consent order); Duofold, Inc., *id.* ¶ 20,773 (1975) (consent order). See also Adolph Coors Co. v. FTC, 497 F. 2d 1178 (10th Cir. 1974).

140. See Comanor, *supra* note 5, at 1437-38.

141. See Turner, *supra* note 19, at 689, quoted in note 72 *supra*.

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Commission Act equivalent.¹⁴² At the core of the present proposal is the simple concept that, absent manufacturer justification of the sort mentioned in the preceding paragraph, vertical price communications should be judged by the same standards as horizontal price communications. Such a shift in doctrine would eliminate the *Colgate* doctrine and in so doing would bring to the law of vertical price restraints a clarity it has not known for a number of years.

142. See *FTC v. Cement Institute*, 333 U.S. 683, 721 n.19 (1948). It is possible that there is renewed interest in the problem at the FTC. See remarks of Michael Pertschuk, Chairman, FTC, ABA 1979 Antitrust Section Spring Program, in Washington, D.C. (April 6, 1979), summarized in *TRADE REG. REPORTS (CCH)* No. 380, at 8 (April 9, 1979).