

## Leegin, the Rule of Reason, and Vertical Agreement

Herbert Hovenkamp\*

### Introduction

Unlike horizontal agreements among competitors, which are relatively uncommon, vertical agreements between actual or would-be suppliers and customers are everywhere. Sales, licenses, franchises, employment agreements, and information arrangements are commonplace. Their very ubiquity indicates that only a few will be of antitrust concern.

Obviously, the ordinary sales contract fixes the transaction price, but it does not restrain trade; indeed, without it, trade would be impossible. The transmission of information from an expert to an insurer may influence the insurer's decision about coverages to offer or reimbursements to make, but no restraint would ordinarily arise, even if an agreement were thought to be present.

While there is a wide array of possible vertical agreements, the concern here is agreements between a manufacturer and its dealers or other customers concerning (1) dealer resale prices, (2) territories or customers, or (3) purchases of other products from that manufacturer or from its rivals. "Resale price maintenance" is the term for the first category; "restricted redistribution" is the term for the second category; "tying" and "exclusive dealing" are other words for restraints in the third category. Resale price maintenance agreements, nonprice restrictions on distribution, and exclusive dealing are all judged by the rule of reason. Tying is still said to be unlawful *per se* when the idiosyncratic requirements of tying law are met. To simplify the exposition, we will speak primarily of the parties to these transactions as the "manufacturer" and the "dealer." But the upstream (selling) party could be a supplier of inputs, a distributor, or even a retailer, and the downstream party (buyer) could be a manufacturer procuring an input, or even a consumer purchasing from a retailer.

There are two overlapping policy reasons for being concerned with horizontal "agreements." Neither reason applies in the same way to vertical agreements. *First*, agreements concern us because cooperative action creates a restraint that is not otherwise possible. In the horizontal context, one competitive firm alone cannot fix prices or exclude rivals from the market without rival participation in that exercise. In one sense, the same is true in the vertical area, where a manufacturer obviously cannot fix a dealer's resale price or force a tied product upon the dealer without the dealer's cooperation (although a manufacturer retailing its product can lawfully charge any retail price it wishes). Nevertheless, a purely vertical agreement does not fix marketwide prices unless the parties control the market.

---

\* Ben V. & Dorothy Willie Professor of Law, University of Iowa.

*Second*, horizontal agreements concern us because they may create market power that did not previously exist. The ordinary cartel agreement creates market power by consolidating the price/output choices of firms that otherwise lack power over output or price. Of course, not every agreement between two or more rivals creates significant or even measurable power—such as, for example, in the case of two farmers agreeing to share an expensive piece of equipment or two solo practicing lawyers who agree to share an office.

As a general matter, a purely vertical agreement does not increase anyone's market power, although it may reflect the preexisting power of one party. Indeed, most litigated vertical agreements involve not so much consent or coordination but are a response to the manufacturer's unilateral power to substitute another dealer. Nevertheless, courts have long held manufacturer/dealer agreements on resale prices (and the other matters mentioned earlier) to be “contracts, combinations...or conspiracies” within the meaning of Sherman Act §1.<sup>2</sup> The natural meaning of the statutory phrases and clear precedent give us this starting point: notwithstanding important differences from horizontal agreements, vertical agreements are covered by §1. To be determined are the elements of the requisite “agreement” in the absence of the conventional exchange of promises.

The recurrently litigated questions center on whether refusals to deal create vertical agreements. Of course, there are many refusals to deal in contexts other than vertical agreements. For example, a vertically integrated firm, whether a monopolist or not, may refuse to deal with outside firms. Or a refusal to deal may be incident to a joint venture or even a “boycott.”<sup>3</sup> The refusals to deal that we are concerned with here are those with effects similar to express vertical agreements. There are two basic situations. First, does an agreement arise when a manufacturer secures compliance by announcing that it will continue dealing only with dealers who comply with its specified condition and by ceasing to deal with those who do not? Second, does an agreement arise when a manufacturer terminates one dealer after receiving a complaint from a rival dealer?

There is, of course, an element of artificiality in discussing the existence of an agreement independently of the competitive policies and substantive rules governing resale price maintenance, restricted distribution, tying, and exclusive dealing. When antitrust tribunals are sensitive to the full range of relevant interests in ruling about the legality of these arrangements in particular cases, there might seem little reason to worry very much about the existence of an agreement: any reasons for denying the presence of an agreement can be fully considered in making the ultimate judgment about legality. And if the reasons for prohibiting or controlling certain conduct are very strong, it makes sense to err on the side of over-inclusiveness in determining the presence of an agreement.

---

<sup>2</sup>E.g., *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911). See 8 Antitrust Law ¶1620 (3d ed. 2010).

<sup>3</sup>See 12 Herbert Hovenkamp, Antitrust Law, Ch. 22 (2d Ed. 2004).

Nevertheless, it is not analytically convenient to consider all topics simultaneously, and the agreement question is commonly considered separately in actual litigation. So we try to consider the agreement concept largely, although not entirely, independently of the agreement's subject. For the same reasons, our analysis concerning the presence or absence of an agreement is largely independent of our own opinions about the legality of the vertical restraints that may result.<sup>4</sup>

### Identifying the Correct Agreement

Given the ubiquity of vertical agreements, we need to be clear on which ones should be of concern to antitrust law. Too many cases have asked whether an agreement is present without considering the nature of the agreement sought. Indeed, virtually every case alleging resale price maintenance or other vertical restraints involves firms who are the parties to *some* agreement. For example, when a dealer alleges unlawful resale price maintenance, it would be pointless to conclude that the agreement requirement is met because the manufacturer and dealer are engaged in buying and selling with each other. That would be tantamount to eliminating the agreement requirement altogether. In *49er Chevrolet* dealers had complained that their contracts with General Motors specified the maximum price that GM would pay for dealer services on vehicles under warranty to consumers or on vehicles damaged in transit.<sup>5</sup> The court found

---

<sup>4</sup>See *id.*, chs. 16-18.

<sup>5</sup>*49er Chevrolet v. General Motors Corp.*, 803 F.2d 1463 (9th Cir. 1986), cert. denied, 480 U.S. 947 (1987). Dealers also agreed not to seek additional compensation from the carriers who had transported the vehicle. See also *Ehredt Underground v. Commonwealth Edison*, 848 F. Supp. 797 (N.D. Ill. 1994), aff'd, 90 F.3d 238 (7th Cir. 1996), cert. denied, 519 U.S. 1056 (1997) (no agreement to require union contractors could be inferred from public utility agency agreement with local telephone company when that agreement explicitly provided that the utility alone would make all such decisions). The claim was subsequently dismissed, 90 F.3d 238 (7th Cir. 1996), cert. denied, 519 U.S. 1056 (1997); *Seagood Trading Corp. v. Jerrico*, 924 F.2d 1555 (11th Cir. 1991) (no antitrust conspiracy between franchisee's fish suppliers and a distributor to limit fish sales could be inferred merely from the fact that low-level employees of the distributor took fish orders from low-level employees of the suppliers).

Cf. *Virginia Vermiculite v. W.R. Grace & Co.*, 108 F. Supp. 2d 549 (W.D. Va. 2000) (concluding that restrictive covenants in gift deeds from a mining firm to a charitable organization satisfied the agreement requirement with respect to claim of conspiracy between the grantor and grantee to cut off a rival mining firm's access to reserves; but that particular agreement was hardly relevant to the alleged antitrust conspiracy; for example, suppose we give Blackacre, which neighbors our gasoline station, to the First Baptist Church subject to a restriction that no gasoline station be operated in Blackacre; the church, intending to use the land for other purposes, happily accepts the gift, but our own purpose is to deny any competitor the right to build a gasoline station on the donated

no antitrust violation, because the agreement merely stated the price that GM would pay for the services it bought; it did not regulate anyone's resale price.

Courts often use the term “unilateral” to state their conclusion that no unlawful agreement exists, but that term can be used in several quite different ways, which need to be untangled. A court may describe a vertical restraint as “unilateral” to express a factual conclusion that the manufacturer adopted the restraint to serve its own interests, conceived without regard to dealer preferences, even though the restraint itself is expressed in a dealer franchise agreement. Another court may describe a restraint as “unilateral” to express a factual conclusion that a manufacturer or dealer did not make any promise or commitment or even communication to the other party. For many courts, finally, the term “unilateral” (or not unilateral) expresses the legal conclusion that the challenged conduct—for example, implementing advance announcements that the manufacturer will cease to supply those who fail to adhere to specified prices—is (or is not) deemed to be a “contract, combination, or conspiracy” for Sherman Act purposes.

A relatively common suit involves a dealer's claim that it was terminated by a manufacturer *because* of its price cutting *pursuant to* the manufacturer's agreement with itself, with dealers generally, or with a specific complaining dealer *about* the plaintiff's prices, prices generally, a complainer's prices, or

---

land; the church has agreed to accept the gift of the land, but it has hardly agreed to exclude our rival from the gasoline market. The distinguishing feature in the Virginia case was that the plaintiff also claimed a sub rosa agreement between commercial interests controlling the charitable organization and the mining defendant; if so, *that* would be the agreement necessary to establish concerted antitrust action). In any event, in later litigation the Fourth Circuit concluded that the mere receipt of a gift deed containing a restrictive servitude did not constitute an agreement with the grantor. *Virginia Vermiculite, Ltd. v. Historic Green Springs, Inc.*, 307 F.3d 277, 282 (4<sup>th</sup> Cir. 2002), cert. denied 538 U.S. 998 (2003):

In the instant case, VVL proffered no evidence that the donation by Grace to HGSI was not a genuine ( *i.e.*, unilaterally given) gift. It often can be difficult to determine whether a purported gift is a gift in fact, or whether it merely disguises bilateral action by which two parties join their resources, rights, or economic power together. But here, VVL simply did not proffer evidence sufficient to raise that difficult question. VVL did not proffer evidence that HGSI joined any resource to Grace's in order to establish the covenants, or to affect the land transfer. Nor did VVL allege that HGSI exercised a right or economic power in consideration for the gift. In other words, insofar as the record discloses, only Grace, not HGSI, exercised any form of right, resource, or economic power....

.... Grace alone had the right and power to attach the covenants. Its unilateral action in doing so was ... beyond the reach of section 1. As a result, we conclude that VVL did not proffer evidence that the defendants “had a conscious commitment to a common scheme designed to achieve an *unlawful* objective....

access to the manufacturer's product. Rather than separating the “because,” “pursuant to,” or “about” questions, a court's discussion of permissible inferences may blend them together. For example, some courts forget to ask the latter two questions when there is sufficient evidence to support a conclusion that the motive for the termination was the plaintiff's price cutting rather than, say, its poor service. Other courts focus on whether the manufacturer acted to implement its own distribution policy, apparently assuming that even price-related terminations involve no agreement unless the manufacturer was induced to serve the anticompetitive interests of complaining dealers as distinct from its own. Yet other courts fail to distinguish a manufacturer's concern for resale prices as such as distinct from a concern about, say, free riding by discounting dealers on the services provided by other dealers.<sup>6</sup>

These several ambiguities infect the cases attempting to apply the determine the criteria for inferring vertical agreements. For example, no agreement among competitors can be inferred from ambiguous circumstances unless they have a motive to coordinate their behavior.<sup>7</sup> That is also true in the vertical context, although we need to define the motive that is relevant. For example, a motive to affect resale prices (1) is not meaningful unless we distinguish resale price control as such from preventing free riding on important services provided by other dealers and (2) is not determinative unless the means for doing so—for example, suggesting resale prices, terminating uncongenial dealers, announcing in advance that noncompliant dealers will be terminated, bowing to the will of a complaining dealer, or implementing resale price agreements with others—is deemed to constitute an agreement for Sherman Act purposes. In short, “motive” should not be considered abstractly.

Illustrating some of the difficulties is the *Helicopter* decision.<sup>8</sup> The Eleventh Circuit ruled that the defendant is entitled to summary judgment unless the plaintiff shows that the alleged conspiracy is “objectively an economically reasonable one” rather than “economically infeasible or irrational.”<sup>9</sup> Correctly understanding that a conspiracy cannot be inferred merely because it would serve the economic interests of the alleged conspirators, the court also ruled that the “plaintiff in a distributor-termination case must also be able to point to evidence which tends to exclude the possibility that the manufacturer was operating independently in making its decision to terminate the distributor.”<sup>10</sup>

---

<sup>6</sup>See 8 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶¶1611-1613 (3d ed. 2010) (in press).

<sup>7</sup>See 6 *id.*, ¶1412.

<sup>8</sup>*Helicopter Support Sys. v. Hughes Helicopter*, 818 F.2d 1530 (11th Cir. 1987).

<sup>9</sup>*Id.* at 1534. The court was relying on Supreme Court summary judgment decisions that considered evidence of horizontal agreements.

<sup>10</sup>818 F.2d at 1534.

Here, “mere complaints” from competing distributors were deemed insufficient to satisfy the second prong of the court's test, which apparently defined the relevant agreement as conduct not serving the manufacturer's own interest (conceived without regard to the complainer's objectives).

In discussing motive, however, the court seemed to be satisfied that the manufacturer had a motive to control the plaintiff's prices (as distinct from a motive to serve the complainer's interests)—namely, that it would profit from its distributor's higher resale prices.<sup>11</sup> But a supplier ordinarily cannot enrich itself by resale price maintenance—for any excess profit resulting from inflated resale prices will accrue to the dealer rather than to the manufacturer.<sup>12</sup> A more plausible reason was offered by the defendant—namely, that the plaintiff “was terminated because it provided inadequate service to local Florida customers.”<sup>13</sup> But even if the motive for termination had been dissatisfaction with the plaintiff's prices, that would not establish any motive for the manufacturer to enter into an agreement with the complainer.

The key point is that the tribunal must first define its concept of an agreement and then ask whether the defendant had a motive to enter into *that* agreement. If unilateral termination of a price cutter because of price cutting does not constitute an agreement, then no agreement exists unless there is a motive for and evidence of the manufacturer's agreement with some third party.<sup>14</sup>

---

<sup>11</sup>Id.

<sup>12</sup>See 8 Antitrust Law ¶1603 (2d ed. 2010).

<sup>13</sup>*Helicopter*, 818 F.2d at 1531.

<sup>14</sup>See *Viazis v. Am. Assn. of Orthodontists*, 314 F.3d 758 (5th Cir. 2002), *cert. denied*, 538 U.S. 1033 (2003) (no conspiracy among orthodontists' association and manufacturer of plaintiff's orthodontic invention could be inferred from the fact that individual orthodontists apparently acting on their own sent complaints to the manufacturer and manufacturer subsequently stopped making the invention); *Imaging Center, Inc. v. Western Maryland Health Sys., Inc.*, 158 Fed. Appx. 413, 2005 WL 3403627 (4th Cir. Dec. 13, 2005) (plaintiff radiologist could not show a boycott agreement between hospitals and their physicians to deny referrals to plaintiff; no evidence that hospitals insisted that doctors not make such referrals; many physicians had expressed concerns about plaintiff's practice, indicating that their decisions were exercises of independent judgment); *HLD Enterp., Inc. v. Michelin North America, Inc.*, 2004 WL 2095739, 2004-2 Trade Cas. ¶74,520 (N.D. Ga. June 29, 2004) (rejecting claim of conspiracy against tire manufacturer that sold tires to large discount price clubs at lower prices than it charged the plaintiffs; the complaint was of unilateral conduct); *Magid Mfg. Co. v. U.S.D. Corp.*, 654 F. Supp. 325, 329 (N.D. Ill. 1987) (“plaintiff must demonstrate that the [defendant] is behaving in a way that is inconsistent with unilateral decisionmaking”).

## Leegin and Vertical Agreements

*Leegin* overturned the longstanding rule of per se illegality for resale price maintenance and applied a rule of reason.<sup>S1</sup> One might think that the question whether a vertical “agreement” exists between a manufacturer and a dealer should not be affected by the mode of analysis to be applied after an agreement is found. First one asks whether an agreement exists, and determines whether the per se rule or rule of reason applies only after receiving an affirmative answer.

But ever since *Colgate* the Supreme Court has generally taken a more restrictive approach on the agreement issue in resale price maintenance cases than in cases involving nonprice restraints.<sup>S2</sup> This was at least partly true because *Colgate* itself involved a criminal indictment for conduct that, at the time, was a per se violation of the antitrust laws.<sup>S3</sup> Under this rule some courts even held that a manufacturer who responded to a powerful dealer's ultimatum to increase rival dealers' prices was acting unilaterally.<sup>S4</sup>

Under the rule of reason such strictness is no longer necessary because anticompetitive effects are no longer inferred from the price agreement alone. For example, if a powerful dealer insists on protecting its margins by asking a supplier to terminate a price-cutting dealer, the only real question is whether the price restraint is initiated freely by the manufacturer in order to control the quality of its dealers and their services, or whether it capitulates to dealer power. In the latter case a finding of agreement is warranted.

In any event, the consequences of not finding an agreement are not quite the same when the underlying restraint is addressed under the rule of reason. Both unilateral and multilateral conduct that result in reduced output and higher prices are actionable, although unilateral conduct must meet the somewhat stricter structural standards of §2's monopolization or attempt offense. Indeed, recent case law exhibits a tendency to apply §2 rather than §1 to other vertical restraints, such as exclusive dealing and tying.<sup>S5</sup> During the *Dr. Miles* era the

---

<sup>S1</sup>*Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 US 877 (2007), *on remand* to 498 F. 3d 486 (5<sup>th</sup> Cir. 2007), overruling *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911).

<sup>S2</sup>*United States v. Colgate & Co.*, 250 U.S. 300 (1919). See also *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 762 (1984).

<sup>S3</sup>See 6 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶¶1438c, d, 1445, 1446 (3d ed. 2010) (in press).

<sup>S4</sup>See, e.g., *Garment District v. Belk Stores Servs.*, 799 F.2d 905 (4th Cir. 1986), *cert. denied*, 486 U.S. 1005 (1988). See 8 *Antitrust Law* ¶1625d (3d ed. 2010) (in press).

<sup>S5</sup>*United States v. Dentsply Intl., Inc.*, 399 F.2d 181 (3d Cir. 2005), *cert. denied*, 536 F.3d 1089 (2006) (applying §2 to exclusive dealing claim); *United States v. Microsoft*

courts often went to great lengths to find that no agreement existed in cases alleging vertically maintained prices. Undoubtedly they were impelled in part by perceptions that the *Dr. Miles* rule condemned too much. But under the rule of reason many resale price maintenance agreements will be found lawful and, in any event, finding the requisite agreement permits the court to go directly to the most important issue, which is competitive effects. As a result, more allowance on the agreement issue seems appropriate under the *Leegin* rule of reason.

Finally, it should be clear that a naked *horizontal* agreement among two or more dealers to force a supplier to discipline a price-cutting rival remains unlawful per se under the same criteria that have always applied in the case of horizontal agreements. In this sense *Leegin* is simply an extension of the Supreme Court's conclusion in *NYNEX* that a *purely* vertical agreement between two firms must be addressed under the rule of reason.<sup>S6</sup>

### Vertical Agreements

The degree of dealer compliance and its relation to the manufacturer's announced condition are usually uncertain. One might presume compliance or require proof of, say, 80 percent of retail sales at the specified price. We recommend the former course. That such compliance is caused by the announcement rather than dealer preference should also be presumed. Announced conditions with regard to tying and exclusive dealing should be presumed to be equivalent in market effect to express agreements.

When we can fairly conclude that the market effects of announced conditions are equivalent to those of express agreements, we can consider the possibility of some kind of "extended" theory of agreement—an implied acceptance of the supplier's terms. The manufacturer's forceful objections that it makes no offer, requests no acceptance, and desires no dealer commitment with respect to goods on hand (which is the only thing the manufacturer cannot unilaterally control through selecting and replacing dealers); that the only understanding is that the parties will continue dealing with each other as long as their views about optimum resale prices coincide; that an announcement merely provides fair

---

*Corp.*, 253 F.3d 34 (D.C. Cir. 2001), *cert. denied*, 534 U.S. 952 (2001) (applying §2 to a potpourri of practices resembling tying and exclusive dealing). See generally Herbert Hovenkamp, *The Obama Administration and §2 of the Sherman Act*, \_\_\_ Boston Univ.L.Rev. \_\_\_ (2010). Cf. *Valuepest.com of Charlotte, Inc. v. Bayer Corp.*, 561 F.3d 282 (4th Cir. 2009) (*Leegin* did not upset traditional rule that a legitimate consignment or distribution agent is not an independent actor).

<sup>S6</sup>*NYNEX Corp. v. Discon*, 525 U.S. 128 (1998). In *NYNEX* the Court went to some lengths to distinguish its earlier decision in *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207, 212 (1959), which had applied the per se rule to an alleged horizontal agreement among appliance manufacturers to boycott the plaintiff retailer at the behest of a competing retailer. See *NYNEX*, 525 U.S. at 134-135.

notice to dealers who might otherwise claim unfair surprise when terminated; and that any conspiracy invented here would be unfair to dealers and lead to harassment of suppliers. These objections may be overcome, albeit with some difficulty.

When these compunctions are overcome, a vertical agreement can be found when there is an announced condition or its equivalent on future dealing, the sanction for noncompliance is credible, and the market effects are proved or presumed to be similar to those of express agreements. Manufacturers cannot fairly claim to be harassed when they announce express conditions, but the proposals outlined here can sometimes be triggered in the absence of announced conditions through pyramiding inferences built on isolated termination(s) found to enforce price control, tying, or exclusive dealing. Lest the extended agreement theories be unduly attenuated, antitrust tribunals should insist on clear evidence about the challenged termination(s).

There is an alternative theory for reaching the announced condition on future dealing: a dealer charging a specified resale price only because of the manufacturer's termination threat surrenders its will to, and thereby "agrees" with, that manufacturer on the resale price. This coerced compliance theory is plausible but suffers from some weaknesses -- namely, doubts that the effects are really the same as those of express contracts and that the "agreement" concept aptly fits the manufacturer's implementation of its will through unilateral power. In addition, adopting a coercion theory may have unsuitable ramifications in other areas. Finally, the coercion theory suffers the embarrassment of not identifying the particular dealer who agreed, because any given dealer's compliance might reflect its personal choice rather than concern for continuing supply. Although this fact bears on who may sue and what must be proved, it is not fatal to all suits. For example, the conclusion that the manufacturer has agreed on resale prices with unnamed dealers adequately supports an injunction in a government equity suit.

If the coercion theory were adopted, a vertical agreement would be found whenever there was an announced condition on future dealing, or its equivalent, with a credible sanction and market effects similar to those of express agreements. The problems of implementation are similar to those accompanying the implied acceptance theory.

### **From *Colgate*<sup>2</sup> to *Monsanto*<sup>3</sup>**

In *Colgate* the Supreme Court held that a manufacturer may refuse to deal with price-cutting dealers and may announce that condition in advance, without thereby entering any agreement with complying dealers. Although this seems inconsistent with any implied acceptance or coercion theory of agreement, no

---

<sup>2</sup>*United States v. Colgate & Co.*, 250 U.S. 300 (1919).

<sup>3</sup>*Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752 (1984).

such theory was presented to the Court.

If the *Colgate* privilege to choose one's suppliers or customers for reasons sufficient to oneself is not absolute, one might read the Court merely to permit a "simple" implementation of one's announced condition on future dealing. A limited privilege would resolve many of the difficulties of the extended agreement theories and allow an agreement to be found in cases of more "complex" enforcement mechanisms supplementing a manufacturer's announcement and implementation of its conditions on future dealing. Such a reconciliation of *Colgate* with the extended agreement theories is mainly consistent with the later Supreme Court decisions both supporting *Colgate* and retreating from it. Mainly, in its 1984 *Monsanto* decision the Court unanimously reaffirmed the *Colgate* principle by declaring that a manufacturer "can announce its resale prices in advance and refuse to deal" with noncompliers and that a dealer "is free to acquiesce...in order to avoid termination." Agreement requires "a meeting of the minds" or a "common scheme," which are not shown by conformity with the specified condition but require evidence that a dealer "communicated its acquiescence or agreement...sought by the manufacturer."

Although *Monsanto* did allow the jury to infer an agreement from admittedly ambiguous evidence falling far short of communicated commitment, the Court also emphasized evidence of directly communicated agreement, and it was very clear that unwilling compliance by dealers to avoid termination does not create an agreement; nor does compliance with a suggestion or announced condition amount to an implied agreement. The plaintiff bears the burden of proving an agreement, and this burden must be taken seriously, the Court suggested, so as not to undercut *Colgate* or the toleration of reasonable nonprice restrictions, which also tend to have price effects. Furthermore, *Monsanto* involved individualized efforts to obtain dealer compliance by means other than simple termination; indeed, the Court found direct evidence of traditional agreement.

Thus, *Monsanto* clearly does not adopt the implied acceptance or coercion theories of agreement, but it may not entirely reject them. Taking *Colgate* as given, *Monsanto* did not pursue agreement concepts. Like the earlier case, *Monsanto* might be read to draw a gross distinction between simple and complex refusals to deal. On the simple and unilateral side of that line would be mere announcement and termination. On the complex and concerted side would be individualized negotiation with dealers, meetings, repeated exhortations, and perhaps the use of third parties (other than to gather information or to effect a termination). Such an interpretation is consistent with the results of *Monsanto*, though not necessarily with its methodology.

Consider such individualized dealings between manufacturer and dealer as reannouncing the condition to particular dealers and informing a dealer that its nonconformity has been observed. Consider also the various forms of giving the dealer a second chance to continue as a customer, persuasion to comply, discussions and negotiation, and communicated assurances of compliance actually or implicitly requested. At least some of these individualized dealings amount to altogether traditional agreements. Indeed, even if such individualized

dealings fall short of fairly traditional express or implied agreements, they might be deemed agreements in another way. These “negotiations” weaken or even remove some of the compunctions against adopting an implied acceptance theory of agreement. A court declining to apply that theory to compliance with announced conditions generally should consider the question anew when confronted with individualized dealings.

To restate the last point in a different way: individualized negotiations could manifest that “complex” enforcement that might exceed the *Colgate-Monsanto* permission for simple implementation of announced conditions on future dealings.

*Schrader’s* used vague language that might permit inferring an agreement from compliance with a manufacturer suggestion or demand in order to avoid termination.<sup>4</sup> In *Beech-Nut*, involving traditional agreements and the use of intermediaries to control retailers, the Court emphasized the policy against resale price maintenance in finding a violation of Federal Trade Commission Act §5.<sup>5</sup> *Bausch & Lomb* found agreements on the basis either of wholesaler involvement in enforcement against retailers or of the “acceptance” by complying dealers of the manufacturer’s plan.<sup>6</sup> *Schwinn* found an agreement on the basis of the manufacturer’s “firm and resolute” insistence that it would terminate noncomplying dealers.<sup>7</sup> To the extent that these cases suggest that mere compliance with the manufacturer’s announced condition creates an agreement via implied acceptance or coercion, they are inconsistent with *Monsanto*.

In *Parke, Davis*<sup>8</sup> the manufacturer negotiated with individual retailers to induce them to comply with specified retail prices and refused to sell to noncomplying retailers and to wholesalers selling to unapproved retailers or to those not complying with specified wholesale prices. The Court found a manufacturer “combination” with wholesalers and retailers. Although there seemed to be traditional agreements between the manufacturer and some retailers with whom it negotiated individually, the Court did not rely on this fact. Rather, it emphasized the use of wholesalers to enforce resale price maintenance and the fact that the manufacturer was not content to obtain compliance with the retail prices it specified through the “voluntary acquiescence” of retailers. However, the Court made clear that no agreement arose merely from dealer compliance motivated by their desire to obtain the product subject to the

---

<sup>4</sup>*United States v. Schrader’s Son*, 252 U.S. 85 (1920).

<sup>5</sup>*FTC v. Beech-Nut Packing Co.*, 257 U.S. 441 (1922).

<sup>6</sup>*United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707 (1944).

<sup>7</sup>*United States v. Arnold Schwinn & Co.*, 388 U.S. 365, 371, 376 (1967).

<sup>8</sup>*United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960).

manufacturer's announced condition on future dealing.

One should not read *Parke, Davis* as fashioning a distinctive rule for inferring agreements with intermediate distributors. If retailer compliance with an announced price condition on future dealing does not create an agreement as a conceptual matter, then wholesaler compliance with an announced condition on approved retailers cannot create an agreement either. The *Parke, Davis* Court did not say that it was creating a special agreement concept for wholesalers. Quite the contrary: it found manufacturer-retailer agreements as well and spoke throughout its opinion of reaching manufacturers who seek retailer compliance by means exceeding announcement of conditions and termination of those who fail to comply.

One can read *Parke, Davis* as implicitly adopting the implied acceptance or coercion theories of agreement, subject to the qualification that simple announcement and termination do not create an agreement. *Colgate* and *Monsanto* might be interpreted the same way. In that event, *Parke, Davis* survives to find agreements where announced conditions are enforced in a "complex" manner. Defining "complex" enforcement is difficult. The category should not include announced conditions, terminations, or the use of third parties to gather information or to effect a termination. It should include control of third-party resales and, more arguably, individualized negotiations with dealers falling short of traditional agreement, and perhaps even exhortation meetings.

One might also regard wholesalers reporting noncomplying dealers to the manufacturer as forming an "information conspiracy" with the latter. However, this theory does not survive *Monsanto*.

Consider also the trouble-ridden *Albrecht* decision,<sup>9</sup> where the Supreme Court found an illegal conspiracy between a supplier and those it hired to solicit and serve the customers of a dealer charging more than the supplier specified. The Court saw a program to obtain the plaintiff's individualized acquiescence, which thus went beyond the privilege of simple announcement and termination. To that extent, the *Albrecht* result can be consistent with the possible reading of *Monsanto* seen earlier.

Many lower courts came routinely to hold that unwilling compliance with another's demands in order to avoid termination created an agreement. This became so common that the Supreme Court's *Albrecht* dicta asserted without discussion that unwilling compliance by a terminated dealer or by dealers generally could establish an agreement. However, this approach is directly contrary to *Monsanto*, which declared expressly that compliance to avoid termination does not create an agreement. More problematically, *Albrecht* also said that it was not frivolous to allege a relevant agreement between a manufacturer and consumers where the manufacturer contracted to sell directly to consumers in order to bypass or coerce a noncomplying dealer. That suggestion does not seem tenable.

---

<sup>9</sup>*Albrecht v. Herald Co.*, 390 U.S. 145 (1968).

Assume that a plaintiff dealer has proved that it was terminated because it never complied with its supplier's resale price demands. Although such proof may gain the tribunal's sympathy, it also demonstrates that the plaintiff never agreed, under any theory, with the supplier. Accordingly, the plaintiff will attempt to show that rival dealers agreed with the manufacturer and that its own termination was related to those other agreements. In particular, the plaintiff will offer three reasons for inferring from its own termination that the manufacturer agreed with others. *First*, it would be futile for the manufacturer to terminate a plaintiff who is not distinctive unless most other dealers are complying. But the performance of other dealers satisfactory to the manufacturer does not itself establish agreements. *Second*, exemplary termination of the plaintiff makes the manufacturer's announced condition a more credible threat. But concrete implementation adds little to the announced condition backed by the presumptively credible threat of termination. In the absence of a generally announced condition, a particular termination may be its equivalent if other dealers are aware of the termination, of the reasons for it, and thus of what they must do to avoid termination. Perhaps these matters can be proven or even inferred from the terminating manufacturer's intent to send a message to its other dealers. But that intent may not itself be inferred merely from terminating the plaintiff.

Nevertheless, explicit and generally circulated manufacturer suggestions, coupled with a termination for disobedience, may fairly be treated as equivalent to an announced condition on future dealing; but compliance with such conditions, if simply enforced, does not create an agreement under *Colgate* and *Monsanto*, although complex enforcement and individualized negotiation might do so. *Third*, the manufacturer pursuing such negotiation or enforcement with respect to the terminated plaintiff may also be doing so with respect to other dealers. We would presume so, unless the supplier explains singling out the plaintiff for individualized negotiation or complex enforcement. The supplier bears the burden of proving that the plaintiff's market situation was distinctive or that the terminating employees were unusually zealous. The proposed presumption is subject to the caveat that the fact finder must be quite confident that the plaintiff was actually terminated for price discounting after individualized negotiation or complex enforcement.

The impact of both *Colgate* and *Monsanto* is significantly reduced by *Leegin*. During the *Dr. Miles* era many resources were used to litigate the agreement issue in resale price maintenance cases because liability commonly turned on it. The likely impact of rule of reason treatment, however, is twofold. First, suppliers will make their RPM agreements more explicit, thus making it clear that an agreement exists, just as typically occurs for the great majority of vertical nonprice restraints such as dealer location clauses. Second, given that the rule of reason applies when an agreement is found, the liability standard may not be altogether different than for monopolization cases under §2 of the Sherman Act. The principal difference will be that the question under §1 will be whether such an agreement "restrains trade," which ordinarily entails a showing of reduced

output.<sup>8.3</sup> By contrast, under §2 the inquiry is whether the practice is undertaken by a dominant firm and unreasonably excludes competitors.<sup>9.4</sup>

### Dealer Complaints

Suppliers have sometimes terminated or otherwise imposed sanctions on a dealer after receiving complaints from that dealer's competitors. The terminated dealer is likely to charge that the manufacturer was implementing a resale price policy through agreement with other dealers. The policy impulses for finding a manufacturer-complainer agreement include the usual one of remedying the injury to a terminated dealer whose only vice, it asserts, was competition. A complaint plus responsive action does not create an agreement in the absence of "acceptance," exchange, or quid pro quo, or perhaps the coercion of one by another.

These dealer-complaint cases have proved difficult for the lower courts because historically they have implicated both horizontal-vertical and price - nonprice ambiguities, as the Supreme Court recognized in *Monsanto*. Because the complainer is objecting to the plaintiff's competition at its own level, terminating the plaintiff is often said to be a "horizontal" restraint. However, most vertical restraints limit "horizontal competition" among distributors of the manufacturer's product. This issue has acquired a somewhat different emphasis since the Supreme Court's *Leegin* decision declaring RPM to be subject to rule of reason analysis.<sup>9.5</sup> A purely vertical agreement setting resale prices is unlawful only if unreasonable in the antitrust sense, while per se illegality may still apply to a properly defined naked horizontal agreement. In any event, it seems clear that an agreement between a *single* dealer and its supplier to terminate a competing dealer because of low prices will be addressed under the rule of reason. However, an agreement among two or more dealers to induce a supplier to terminate a third, price-cutting dealer might be regarded as unlawful per se, and one circuit has accepted that result with respect to the agreement among the dealers standing alone. However, it applied the rule of reason to the agreement among the dealers and the manufacture, following dicta in *Leegin* that appears to command that result.<sup>9.6</sup> In sum, previously the important difference was whether the restraint in question could be classified as "price" or "nonprice." Given *Leegin*, however, the more important distinction is between purely vertical or horizontal agreements.

Courts speaking in these horizontal-vertical terms are attempting to distinguish anticompetitive limitations serving the complainer's interest in excess dealer-level profits from potentially procompetitive limitations serving the

---

<sup>8.3</sup> See Chs. 19-20.

<sup>9.5</sup> *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 US 877 (2007).

<sup>9.6</sup> *Toledo Mack Sales & Service, Inc. v. Mack Trucks, Inc.*, 530 F.3d 204, 224-225 (3d Cir. 2008) (analyzing and condemning this situation).

manufacturer's interest in product promotion, customer services, or the like. Unfortunately, the presence of a dealer complaint does not distinguish one case from the other. Dealers may also share the manufacturer's interest in sale-increasing services. Or the complaint may simply reflect the truism that one dealer cannot profitably comply with the manufacturer's desires for certain services, or for prices facilitating costly services, if rival dealers without such services sell the same product for less.

Historically, manufacturer control of a dealer's resale price was treated much more severely than control of resale territories, customers, services, and other "nonprice" matters. Whether that continues to be true under *Leegin* is unclear at this writing, although we recommend closer scrutiny of vertical price agreements than of nonprice agreements. Obviously, however, even permissible nonprice restraints usually affect prices. For the same reason, a complaint and a termination can obviously affect price and yet merely implement lawful customer or territorial agreements assuring resale services. This can be equally true when the manufacturer has no formal pre-complaint policy of limiting distribution.

A curiosity of many dealer-complaint cases is their failure to identify the nature and content of the alleged complainer-manufacturer agreement. The apparent subject matter of the alleged agreement is not the plaintiff's destruction but the manufacturer's distribution policy and its implementation, the complainer's future behavior, or both.

In *Monsanto* the Supreme Court ultimately supported a jury finding of vertical price agreements between Monsanto and nonterminated dealers without regard to the complaints from some of them about the plaintiff. The complaints were used simply as one of several elements supporting the jury decision that the plaintiff's termination was attributable to price discounting rather than to inadequate representation. The plaintiff's damage case was then completed by the Court's inference that terminating discounters was either part of, or pursuant to, the price agreements with others.

The unanimous decision is important for the clarity with which the Court separated these several issues, for the policy premises it articulated, and for the legal test that emerged from those premises. The Court's policy premises were twofold: the elusiveness in fact of the law's distinctions and the appropriateness of information movements and consultations between a manufacturer and its dealers. Because nonprice restraints affect prices, one must be wary about using price-related complaints as evidence of vertical price agreements. Because dealer-manufacturer information exchanges are natural and often unavoidable aids to efficient distribution, inferring conspiracies from them would unfairly interfere with rational distribution.

These considerations led the *Monsanto* Court to hold that termination after or "in response to" complaints does not show a conspiracy. To get to the jury, the burden remains on the plaintiff to introduce additional evidence tending to exclude the possibility of independent action by the manufacturer and other dealers. As the Court earlier made clear in discussing the *Colgate* issue,

“independent” action for this purpose includes acquiescence in another’s “demand in order to avoid termination.”

At one time some courts allowed juries to find a manufacturer-complainer conspiracy merely from termination “after” a complaint. This proposition is unsound in principle, and most lower courts have rejected it. “After” does not mean “because.” Totally unconnected with a complaint, for example, would be a termination based on independent grounds, such as nonpayment, or on facts stated by the complainer but already known to the manufacturer. Perhaps the courts allowing the inference meant to shift to the manufacturer the burden of rebutting a causal connection between complaint and termination. But the case for such a shift is not compelling, and *Monsanto* held that the plaintiff has the burden of showing more than that termination followed a complaint.

Most of the lower courts required a causal connection between the complaint and the plaintiff’s termination. They insisted that the termination be “in response to” the complaint but usually without distinguishing two different kinds of responsive termination. A termination can be responsive in that the complainer coerces the manufacturer to adopt a restrictive distribution policy, or it can be responsive in that the complaint provides the information leading the manufacturer to terminate the plaintiff in implementing its own policy. Some courts found responsiveness in little more than a termination after the complaint. A few courts explained responsiveness in terms of providing the information triggering the termination and thus aiding or abetting the manufacturer in implementing a restrictive distribution policy.

Further, termination responses reflecting the manufacturer’s own distribution policy differ greatly from those imposed upon it by a complaining dealer. In the latter case, the manufacturer’s compliance with the complainer’s demand is more likely to be anticompetitive. The lower courts had apparently adopted the principle that coercion of the manufacturer creates an agreement but without determining how it might be proved. The argument for shifting to the manufacturer the burden of disproving coercion is not persuasive and may be precluded by *Monsanto*. Coercion seems presumptively absent when the manufacturer has a pre-complaint restricted distribution policy. Even without such a policy, the complaint may bring facts or arguments to the manufacturer’s attention, which lead the manufacturer, in the exercise of a unilateral judgment, either to adopt such a policy or to conclude that a general policy is unnecessary but that the plaintiff dealer has “gone too far.” The complainer’s bargaining power relative to the manufacturer is relevant but elusive. It need only be sufficient to persuade the reluctant manufacturer that it would lose less by terminating the plaintiff than by losing the patronage of the complainer and perhaps of other silent dealers who share the complainer’s sentiments. Also illuminating, and elusive, are the “objective” merits of restricting distribution for a supplier in the defendant’s position.

Even if we could determine that a manufacturer terminated a plaintiff dealer solely because it felt compelled to placate a complainer, *Monsanto* seems to reject the coercion premise for finding an agreement. If dealer compliance to

avoid the manufacturer's refusal to deal does not create an agreement, then manufacturer compliance to avoid the complainer's refusal to deal would also fall short of an "agreement," unless the greater threat to competition demands a different result. A different result is not permitted if *Monsanto* and *Colgate* rest on a narrow agreement concept or on policies of free choice or of administrability that are also triggered when a dealer announces conditions on its future dealing. *Monsanto* may, however, allow an agreement finding when the complainer engages in "complex enforcement" of its announced conditions.

One might see the complaint as an assurance by the complainer of its own future compliance, the termination as an assurance by the manufacturer of its commitment to resale price maintenance, or both parties' behavior as evidence of a preexisting agreement between them. However, these possibilities are entirely speculative in view of the many other possible interpretations of the complaint and the termination. As a legal matter, moreover, *Monsanto* raises several insuperable barriers to finding a tacit meeting of the minds in these circumstances. A communicated assurance does not create an agreement unless it is sought. Beyond that, the Court made clear that the jury may not infer an agreement from a complaint and even a responsive termination. *Additional* evidence is required. To be sure, the Court said that admittedly ambiguous evidence supported the jury verdict, but this was in the context of direct evidence of a traditional agreement and of price stabilization efforts beyond mere announcement and implementation of conditions on future dealing.