

**ABA BUSINESS LAW SECTION
ANTITRUST LAW COMMITTEE**

2019 Annual Meeting, Washington, D.C.
September 2019

**Annual Antitrust Update for Business Lawyers:
Vertical Relationships & Vertical Restrictions**

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I. VERTICAL RELATIONSHIPS AND ANTITRUST LAW

The criminal antitrust laws draw a clear line against anticompetitive horizontal restraints—i.e., cartel activity that involves price-fixing, bid rigging, or the allocation of customers or markets among competing firms. The standards governing the review of horizontal mergers of competing firms are the subject of detailed guidance and precedents created by reviewing agencies. In contrast, the boundaries of the antitrust constraints on vertical relationships and vertical restrictions imposed by entities at different levels of the supply chain are less clear. In some instances, antitrust laws may appear to operate in ways that appear arbitrary and unpredictable to business people. Indeed, as buying and selling systems and technologies grow more complex, the line between lawful and unlawful conduct may be difficult for experienced antitrust practitioners and even Supreme Court justices to discern. Further complicating matters are divergences between federal and state law, and between U.S. and non-U.S. law, in their treatment of vertical relationships and supplier-imposed restrictions on sales and distribution by resellers.

Notable antitrust developments in the first six months of 2019 exemplify the difficulty of predicting outcomes and the high cost of getting it wrong when vertical restrictions are alleged to be anticompetitive.

- **The FTC Successfully Challenges Qualcomm’s Patent Licensing Policy**

In May 2019, the Federal Trade Commission won an injunction against Qualcomm’s “no license, no chips” policy, under which customers were required to obtain expensive patent licenses in order to buy Qualcomm chips that allow U.S. smartphones to connect to wireless networks. The ruling also ordered Qualcomm to change its policy of exclusively licensing its standard-essential patents (SEPs) to end manufacturers while refusing to license to rival chipmakers. Qualcomm’s appeal to the Ninth Circuit is now pending. Qualcomm has also been targeted by authorities in other jurisdictions, including the European Union, which fined the company €997 million (\$1.22 billion) in 2017.

- **EU fines MasterCard €570 million for Restricting Merchants’ Access to Cross-border Card Payment Services**

On January 22, 2019, the European Commission announced in a [press release](#) that it had fined MasterCard €570,566,000 (nearly \$650 million) for preventing merchants from taking advantage of lower interchange fees offered by banks located within the Single

Market but outside the country where the merchants are located. Prior to December 9, 2015, when the [Interchange Fee Regulation](#) introduced caps, retailers in high-interchange fee countries could not benefit from lower interchange fees offered by banks located in another Member State. In April 2013, the Commission [opened a formal investigation](#) against MasterCard to assess whether its restrictions against “cross-border acquiring” violated EU antitrust rules. The Commission found that the restrictions caused retailers to pay more for bank services to receive card payments than if they had been free to shop around for lower-priced services, which in turn led to higher prices for consumers, less cross-border competition, and an artificial segmentation of the Single Market.

- **European Commission Fines Google Nearly \$1.7 Billion for Abusive Practices in Online Advertising**

In a press release issued March 20, 2019, the EC announced its decision to fine Google LLC €1.49 billion (approximately US\$1.7 billion) for illegal abuse of Google’s dominant position in the market for online search advertising intermediation. After an investigation that began in 2016, the Commission found that Google maintained its dominant position and effectively prevented competitors such as Microsoft and Yahoo from competing in the online ad market by means of exclusive dealing contracts and other contractual requirements imposed on website publishers. As noted in the press release, this is the third time since 2017 that the EU has levied a multibillion dollar fine on Google for anticompetitive practices.

In the realm of private antitrust litigation, in a closely-watched case a 5-4 majority of the U.S. Supreme Court held that a consumer class of iPhone app buyers had standing to sue Apple for anticompetitive sales and distribution practices. In May 2019, affirming the judgment of the Ninth Circuit, the Supreme Court ruled that consumers who purchased iPhone apps from Apple’s “App Store” had standing as direct purchasers to bring antitrust claims against Apple for allegedly monopolizing the sale of the apps and charging higher-than-competitive prices. Writing for the majority, Justice Kavanaugh rejected Apple’s argument that consumers were not direct purchasers for purposes of the *Illinois Brick* doctrine because independent developers set the prices at which the consumers purchased the apps from Apple. The case is *Apple Inc. v. Pepper*, 139 S. Ct. 1514 (2019).

The divergence of views regarding when vertical relationships violate the antitrust laws even extends to mergers. A notable antitrust case decided this year involved a government challenge to a vertical merger, AT&T’s acquisition of Time Warner. On February 26, 2019, in *U.S. v. AT&T*, ___ F.3d ___ (D.C. Cir. Feb. 26, 2019), the United States Circuit Court of Appeals for the District of Columbia rejected the Department of Justice Antitrust Division’s appeal from the lower court decision clearing the proposed transaction. The appellate court cited evidence of dynamic competition from emerging content providers such as Netflix and Hulu, and the failure of the government to contend with the defense expert’s analysis of real-world data for prior vertical mergers in the industry, which showed “no statistically significant effect on content prices.” DOJ declined to appeal. The opinion shed little new light on the standards to apply to similar transactions.

In the absence of bright line rules, it is important to understand how antitrust laws may bear on certain key aspects of vertical relationships. Toward that end, this article combines an overview of the relevant statutes and selected cases with practical takeaways for business law practitioners working in-house or as outside counsel to firms buying and selling in the U.S. and elsewhere, online and in stores, and in closed and open distribution systems.

II. “VERTICAL PRICE-FIXING” – RESALE PRICE MAINTENANCE (RPM)

A. *The Rule of Reason Standard Determines Whether RPM Agreements Are Unlawful Restraints on Trade*

Under a vertical resale price maintenance (RPM) agreement, the supplier of a product and its downstream dealer or distributor agree on the price at which the dealer or distributor may resell the product to its customers.

A minimum resale price maintenance (RPM) agreement exists when a reseller agrees to sell at or above a certain price dictated by its supplier. Some minimum RPM agreements mandate selling at a fixed price, while others may require the reseller to ensure that any discounting does not exceed a certain percentage off the supplier’s resale price list.

Maximum RPM agreements ensure that resale prices remain at or below a certain level. Maximum RPM agreements are evaluated under the rule of reason, as they may be more likely to benefit, rather than harm, consumers. *State Oil Co. v. Khan*, 522 U.S. 3 (1997). As a practical matter, maximum resale price constraints are rarely the subject of legal challenges or regulatory action.

The treatment of minimum RPM under U.S. antitrust law has drawn considerable attention since the Supreme Court’s majority decision in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.* 551 U.S. 877 (2007) (“*Leegin*”) held that minimum RPM agreements would no longer be treated illegal per se but should be assessed under the rule of reason. Thus, in addition to focusing on whether conduct reflects a price-fixing agreement (or, e.g., merely a unilateral pricing suggestion), courts must now engage in a fact-intensive consideration of relevant market definition and market power, and a balancing of the agreement’s procompetitive and anticompetitive effects.

In dual distribution situations—in which the supplier may be in competition with its own dealers for retail sales of the supplier’s product—RPM would ordinarily viewed as a vertical price restraint, not as a horizontal price-fixing conspiracy, as long as the supplier, and not a combination of competing resellers, was the source of the restraint. *See Spahr v. Leegin Creative Leather Prods., Inc.*, 2008 WL 3914461, **6-7 (E.D. Tenn. 2008) (rejecting claim that accessories manufacturer’s dual distribution system transformed its resale price agreements into per se unlawful horizontal price-fixing agreements) (citing *International Logistics Group, Ltd. v. Chrysler Corp.*, 884 F.2d 904, 906 (6th Cir. 1989), *cert. denied*, 494 U.S. 1066, (1990)).

B. *Conflicting Treatment of RPM Under Federal and State Law*

Notwithstanding the change in federal law wrought by *Leegin*, minimum RPM is still per se illegal in some states, including California and Maryland. *E.g.*, MD. COMM. CODE § 11-204; *California v. DermaQuest Inc.*, No. RG10497526 (Cal. Sup. Ct., Feb. 23, 2010). In February 2010, the California Attorney General filed an action under alleging that a beauty products manufacturer violated the Cartwright Act by entering into minimum RPM agreements with resellers, which the complaint alleged were per se illegal under the relevant state law. DermaQuest entered into a Consent Decree less than a month later, in which it repudiated the agreements at issue, agreed not to enter into future RPM agreements, and paid \$120,000 in civil penalties and legal costs. *See* 98 Antitrust & Trade Reg. Rep. (BNA) 316 (Mar. 12, 2010).

In New York, minimum RPM agreements are unenforceable but not per se illegal under N.Y. General Business Law § 369-a, the state Fair Trade Act repealer, which provides that “contracts” between manufacturers and retailers fixing resale prices are “unenforceable.” See *New York v. Tempur-Pedic International, Inc.*, 30 Misc. 3d 986 (N.Y. Sup. Ct. 2011), *aff’d*, 944 N.Y.S.2d 518 (1st Dep’t 2012).

B. Compliance Implications of Divergence in the Treatment of RPM

The divergent approaches to RPM complicate antitrust counseling in this area. Federal constraints on such agreements have loosened significantly but in some states (e.g., California), in some industries (e.g., mass-marketed consumer goods), and in some circumstances (e.g., where disgruntled retailers lodge complaints), the establishment of a resale price agreement may expose the supplier to disruptive private claims and public enforcement efforts. Furthermore, in many non-U.S. jurisdictions RPM is presumptively illegal. For these reasons, many practitioners advise that the most prudent approach is to forgo RPM altogether and instead deploy recommended resale prices, a unilateral no-discounters policy, or restraints on minimum advertised prices.

C. Unilateral Conduct and the Colgate Doctrine

In the U.S., so-called *Colgate* policies aid suppliers in discouraging excessive discounting of the supplier’s products without the risks associated with RPM. A large body of pre- and post-*Leegin* case law, starting with *United States v. Colgate & Co.*, 250 U.S. 300 (1919), addresses when a threat to terminate or a refusal to deal with price discounters is permissible unilateral conduct, and when such conduct evidences a resale price agreement. In *Colgate*, the Supreme Court upheld a supplier’s right to “exercise his own independent discretion as to parties with whom he will deal.” Thus, it is not unlawful to refuse to deal with or, in the absence of some other legal constraint, to terminate relationships with discounters, as long as the refusal to deal or termination is the result of supplier’s own independent, unilateral decision-making.

This principle was reaffirmed and expanded upon in *Monsanto Co. v. Spray-Rite Serv. Co.*, 465 U.S. 752 (1984), in which the Supreme Court recognized that independent, unilateral acts to influence minimum resale prices—when the supplier has not sought or accepted an agreement from its retailers—do not amount to a RPM contract. Following *Monsanto*, other courts have likewise distinguished between unilateral conduct and RPM agreements, e.g.:

- *In re Disposable Contact Lens Antitrust Litigation*, 215 F. Supp. 3d 1272 (M.D. Fla. June 14, 2016) (vertical agreements were established by evidence of communications between non-discount resellers, their distributor, and contact lens manufacturers regarding the enactment, implementation, and enforcement of unilateral price policies, as well as direct evidence of actual negotiations and an “agreement” between one manufacturer and a discount retailer).
- *United States v. Parke, Davis & Co.*, 362 U.S. 29, 45 (1960) (evidence of an agreement found where wholesalers were directed by Parke Davis “to stop the flow of Parke Davis products to the retailers, thereby inducing the retailers’ adherence to its suggested retail prices”).
- *Australian Gold, Inc. v. Hatfield*, 436 F.3d 1228 (10th Cir, 2008) (no RPM agreement established where distributor agreement reserved the supplier’s right to terminate distributor for failure to comply with the supplier’s unilateral minimum RPM policy;

further, “[t]he agreements specifically state that ‘ETS does not request and will not accept Distributor’s agreement to comply with any such suggested price . . .’”).

- *Acquaire v. Canada Dry Bottling Co.*, 24 F.3d 401 (2d Cir. 1994) (“[e]vidence of pricing suggestions, persuasion, conversations, arguments, exposition, or pressure is not sufficient to establish the coercion necessary to transgress § 1 of the Sherman Act”; no RPM agreement established by supplier’s conditioning participation in a promotional discount program on distributors’ adherence to suggested retail prices and use of supplier’s invoicing form disclosing to retail customers both the suggested resale price and wholesale price).
- *Jeanery, Inc. v. James Jeans, Inc.*, 849 F.2d 1148 (9th Cir. 1988) (“putting pressure on a retailer,” including a threat not to deliver goods, is “consistent with the privilege of independent action permitted a manufacturer under *Colgate*”).
- *Isaksen v. Vermont Castings, Inc.*, 825 F.2d 1158 (7th Cir. 1987) (no RPM agreement is established merely by providing suggested price list to distributors, but evidence of threats to “mix up” retailer’s orders if it did not raise prices, followed by compliance, could support finding the requisite agreement).
- *Jack Walters & Sons Corp. v. Morton Bldg., Inc.*, 737 F.2d 698, 707 (7th Cir. 1984) (direct advertising of suggested resale prices by manufacturer engaged in dual distribution was “perfectly lawful”).
- *See also State of New York v. Tempur-Pedic Int’l*, 2011 WL 198019 **5-6 (N.Y. Sup. Jan. 14. 2011) (ruling that proof of an RPM contract was lacking, where supplier communicated its unilateral minimum price policy to retailers, but evidence failed to show “that interactions between Tempur-Pedic and its retailers amounted to a meeting of the minds or consisted of harassment, threats to harm business, or concerted acts between Tempur-Pedic and its retailers to harass other noncompliant retailers”), *aff’d*, 944 N.Y.S.2d 518 (1st Dept. 2012).

The checklist below identifies some of the key elements of a bona fide, unilateral *Colgate* policy:

A COLGATE POLICY 10-POINT CHECKLIST

1. Is the policy set forth in a standardized written communication addressed to all resellers?
2. Do the client’s internal documents and the policy itself recite credible procompetitive reasons for minimum pricing (or maximum discounts), such as maintaining a premium brand image and consumer goodwill, encouraging dealer investments in promotion and services, discouraging free riding, or otherwise promoting interbrand competition?
3. Does the policy expressly state that it is the supplier’s unilateral policy, subject to unilateral amendment or withdrawal at the supplier’s sole discretion?
4. Does the policy reiterate that resellers may set their own resale prices? (*E.g.*, “This Policy is not a restriction against selling at any particular price. You are free to establish the prices at which you sell our Products and we will neither seek nor accept any agreement with respect to such resale prices.”)

5. Does the policy disclose that the consequences for noncompliance will be discontinuance of sales to the noncompliant reseller?
6. Is the policy enforced in good faith, and are all related communications truthful and, ideally, reviewed by counsel before sending?
7. Is the policy reviewed and recirculated to resellers on at least an annual basis?
8. Does the policy state that no employee of the supplier is authorized to negotiate or vary the terms of the policy?
9. If there are written reseller agreements, do the termination provisions of those agreements allow unilateral termination or nonrenewal by the supplier without cause upon written notice to the reseller?
10. Does the policy designate an appropriate company contact to whom all questions or concerns regarding the policy should be directed in writing?

In contrast, the risk that a “unilateral” policy may be challenged as a de facto RPM agreement increases when one or more “red flags” such as the following are present:

COLGATE POLICY “RED FLAGS”

1. Is the supplier adopting the policy at the behest of one or more retailers?
2. Has the supplier solicited input from one or more retailers on the terms of the policy before or after its adoption?
3. Has a retailer provided the supplier with a suggested form of unilateral policy?
4. Are the products covered by the policy mass-marketed consumer goods that require little to no investment in point-of-sale services?

III. MINIMUM ADVERTISED PRICE (MAP) RESTRICTIONS

Minimum advertised price (MAP) restrictions govern the advertising or display of price information by resellers, but do not control the actual resale price. For this reason, MAP agreements are treated under the U.S. antitrust laws as non-price vertical restraints, which are subject to the rule of reason. *See Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 54-55 (1977) (“Vertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of his products. These “redeeming virtues” are implicit in every decision sustaining vertical restrictions under the rule of reason.”); *Blind Doctor, Inc. v. Hunter Douglas, Inc.*, No. C-04-2678 (MHP), 2004 WL 1976562 (N.D. Cal. Sept. 7, 2004) (recognizing that price advertising restrictions must be assessed under the rule of reason).

MAP programs under which retailers must adhere to price advertising restrictions (i.e., advertising resale prices at or above a fixed minimum or no prices at all) in order to receive cooperative advertising funds from the supplier have long been upheld by U.S. courts and the FTC. *E.g.*, *In re Nissan Antitrust Litigation*, 577 F.2d 910 (5th Cir. 1978), *cert. denied*, 439 U.S. 1072 (1979); *Clinique Lab., Inc.*, 116 F.T.C. 126 (1993); FTC Statement of Policy Regarding

Price Restrictions in Cooperative Advertising Programs, 6 Trade Reg. Rep. (CCH) ¶ 39,057 (FTC, May 21, 1987).

MAP programs can be challenged on the grounds that they effectively eliminated the retailer's practical ability to set its own price (and were therefore per se illegal or unenforceable RPM agreements) or because they otherwise impeded or eliminated competition. *See, e.g., In re Time Warner*, Commissioners' Statement at <http://www.ftc.gov/os/2000/05/cdstatement.htm> (explaining that music distributors' MAP policies, while not amounting to RPM agreements, were nonetheless unlawful under a rule of reason analysis, where the five distributors together accounted for over 85% of the market, and each had market power in that no music retailer could realistically choose not to carry the music of any of the five major distributors; MAP policies were adopted by each of the distributors for the purpose, and in fact had the effect, of stabilizing retail prices with consequential effects on wholesale prices, ending price competition that had previously existed, compliance with the MAP policies effectively eliminated the retailers' ability to communicate discounts to consumers and financial incentives ensured that retailers had little incentive to actually sell product at a discount).

Where a supplier's MAP restrictions expressly permit the retailer to sell at prices set by the retailer, and where in fact discounted sales actually do take place, there is a low risk that a MAP policy or agreement will be actionable as an "unreasonable" restraint on trade. *See U.S. Pioneer Elecs. Corp.* 115 F.T.C. 446 (FTC 1992) ("Unilaterally terminating a dealer for advertising below suggested prices is less competitively threatening to interbrand competition than unilaterally terminating a dealer for failing to follow a suggested resale price.").

IV. TREATMENT OF RPM AND MAP RESTRICTIONS IN OTHER JURISDICTIONS

Canada

Section 76 of the Canadian Competition Act permits the Competition Tribunal to make remedial orders against three types of "price maintenance" conduct, where that conduct has had, is having or is likely to have an adverse effect on competition in a market:

- where a person influences upward or discourages the reduction of the price at which another person supplies, offers to supply or advertises a product within Canada;
- when a person refuses to supply or otherwise discriminates against another person because of the low pricing policy of that person; and
- when a person induces a supplier to refuse to supply a product to another person because of the low pricing policy of that person.

The enactment of these provisions in 2009 decriminalized RPM in Canada, bringing the law more closely in line with the U.S., except that RPM and refusing to deal with discounters are specifically identified as potentially reviewable, albeit no longer criminal, practices.

In 2014, the Competition Bureau issued its *Price Maintenance (Section 76 of the Competition Act) Guidelines*. *See* Canadian Competition Bureau, [Price Maintenance \(Section 76 of the Competition Act\) Guidelines](#) (Sept. 15, 2014).

The Guidelines note that “[a]n important requirement under section 76 is that price maintenance conduct has had, is having or is likely to have an adverse effect on competition in a market, which is only likely to occur in some circumstances.” The Guidelines state further that adverse effects on competition due to RPM—

may occur, for example, if price maintenance conduct resulted in the exclusion of rivals or new entrant competitors to the supplier or the exclusion of discount or more efficient retail competitors. It may also occur if price maintenance conduct was being used to inhibit competition among suppliers or retailers.

When examining whether price maintenance conduct is likely to adversely affect competition in a market, market power is a key factor in the Bureau’s analysis. In a general sense, market power is the ability of a firm (or group of firms) to profitably maintain prices above the competitive level, or other elements of competition, such as quality, choice, service or innovation, below the competitive level, for a significant period of time. Where price maintenance conduct is unlikely to create, preserve or enhance market power, the conduct is unlikely to have an adverse effect on competition in a market. [*Guidelines*, § 1.]

As a general rule of thumb, in the absence of unusual features in a market, the Bureau is unlikely to find that a company with less than 35% market share has market power. *Guidelines*, § 5.2.

Among other things, the Guidelines state that supplier’s suggestion to a reseller of a minimum resale price would be viewed as proof that the reseller has been “influenced” in its pricing, unless the supplier establishes that it made clear to the reseller that it had no obligation to accept the suggestion and would not suffer in its business relations with the supplier or with any other person if it failed to follow the suggestion. *Guidelines*, § 5.2.

Even when it was a criminal offense, RPM was historically a low enforcement priority in Canada, and since the Guidelines issued, there have been no noteworthy cases against which to test whether the outcome would be similar under U.S. law.

European Union

The competition rules of the European Union diverge significantly from U.S. antitrust law in the treatment of RPM and MAP policies and territorial and customer restraints. In contrast to the more lenient approach of the rule of reason, the EU and its member states restrict such practices and impose severe monetary penalties against noncompliant firms.

The EU’s overall competition regime is shaped by the Treaty on the Functioning of the European Union (TFEU), regulations adopted by the Council or the European Commission, and various notices, guidelines, and other interpretive documents, which explain in more detail the Commission’s policies relating to the interpretation of its substantive rules. Similar to Section 1 of the Sherman Act, Article 101(1) of the TFEU prohibits agreements that appreciably restrict or distort competition. If an agreement appreciably restricts competition, it is null and void according to Article 101(2), subject to Article 101(3), which permits restrictive agreements when their benefits outweigh their anticompetitive effects.

Standing alone, the TFEU would require a fact-intensive, case-by-case assessment of every vertical restriction to determine whether it appreciably restricts competition and, if so, whether its

benefits outweigh its anticompetitive effects. The European Commission's Block Exemption Regulation on Vertical Agreements and Guidelines on Vertical Restraints, however, designate safe harbors for many vertical restrictions by making Article 101(1) inapplicable to "de minimis" restrictions that have no appreciable impact on competition and vertical agreements in which neither the buyer nor the seller has a market share exceeding 30%. *See* Regulation (EU) No 330 of April 20, 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices (2010) O.J. (L 102) [hereinafter, "Block Exemption Regulation"]; *See* Guidelines on Vertical Restraints (2010) O.J. (C 130/1) [hereinafter, "Vertical Restraint Guidelines"].

As stated in the Vertical Restraint Guidelines, Article 2(4) of the Block Exemption Regulation explicitly excludes from its application vertical agreements entered into between competing undertakings, which are addressed in the Vertical Restraint Guidelines on the applicability of Article 101 to horizontal cooperation agreements. A useful practical guide to compliance with the Block Exemption Regulation is "The Competition Rules for Supply and Distribution Agreements," published by the Office of the European Union in 2012, available at <https://publications.europa.eu/en/publication-detail/-/publication/c06dce20-7a0f-4611-b767-db9a5aa77f2c/language-en>.

At the same time, Article 4 of the Block Exemption Regulation contains a list of "hardcore restrictions" for which there is a heavy presumption of illegality and no safe harbor based on market share. Enforcement against hardcore vertical restrictions is a high priority in the EU, and compliance counsel should therefore ensure that managers and employees are aware of what is and is not prohibited.

Article 4(a) of the Block Exemption Regulation provides that vertical agreements that restrict the buyer's ability to determine its resale price are presumed to be incompatible with Article 101(1) of the TFEU. The hardcore designation applies to direct and indirect restrictions on resale pricing, bringing within its scope any mechanism that interferes with the reseller's ability to set its own prices. The Vertical Restraint Guidelines list various examples of indirect RPM agreements, including agreements fixing the distribution margin, fixing the maximum discount the distributor can grant from a prescribed price level, making the grant of rebates or reimbursement of promotional costs by the supplier subject to adherence to a given price level, linking the prescribed resale price to the resale prices of competitors, threats, intimidation, warnings, penalties, delay or suspension of deliveries or contract terminations in relation to observance of a given price level. Vertical Restraint Guidelines, § 3, ¶ 48.

The Block Exemption Regulation allows the possibility of overcoming the presumption of illegality only in narrow circumstances, such as when used on a short-term basis to aid a new business in starting up. To date, there have been no published decisions in which the benefits of a resale price maintenance agreement have been found to outweigh its presumed anticompetitive effects.

Maximum resale price restrictions are not hardcore restrictions unless they effectively act as an indirect mechanism for maintaining minimum resale prices. Recommending resale prices is allowed, but applying any sort of "pressure" to the reseller is prohibited, as is the offering of incentives or disincentives tied to the reseller's adoption of recommended resale prices.

EU competition rules make less of a distinction between RPM and minimum advertised price (MAP) restraints than does U.S. antitrust law. MAP restrictions may be viewed—particularly in the context of online retailing—as improperly dictating retail prices by limiting the retailer's

ability to inform customers of available discounts, thereby removing an incentive for price competition between retailers. For this reason, compliance counsel should carefully review any proposed restriction that seeks to influence resale pricing and any communications with EU distributors and resellers that concern resale prices or the advertising of resale prices.

China

The Chinese Anti-Monopoly Law expressly prohibits suppliers from fixing resale prices or dictating minimum resale prices. At the same time, other provisions of the law arguably allow a supplier to offer proof that the benefits of its conduct outweigh any anticompetitive effects under the set of exemptions for any agreement (not just RPM) that promotes technological improvement, research and development, efficiency or the public interest.

In recent years, RPM has been a high enforcement priority of the Chinese antitrust agencies, which have brought cases against a number of companies, alleging they engaged in presumptively illegal RPM, as to which none of the exemptions applied. In contrast, in cases where private plaintiffs have challenged alleged RPM—including an influential 2014 decision by the Shanghai High Court—the courts appear to have taken an approach something like a rule of reason, placing a heavier burden of proof on the plaintiff.

In late 2017, in the first case involving judicial review of an agency proceeding against a company for engaging in RPM, the Hainan High People’s Court issued a decision that upheld the relevant agency’s sanctions under an EU-like “prohibition in general, exemption in individual” standard. Engaging in RPM in China therefore may incur a high degree of risk. As in the EU, however, the use of unilaterally recommended prices is a generally permissible alternative.

V. PRICE PARITY RESTRICTIONS

Most favored customer (or “most favored nation”) price parity restrictions are assessed under the rule of reason and generally of little antitrust concern if the party imposing the price parity term lacks market power. Indeed, courts generally approve of agreements under which a buyer successfully bargains with a seller for the lowest price or a price no lower than that charged by the seller to its competitors. *E.g.*, *Blue Cross & Blue Shield United of Wis. v. Marshfield Clinic*, 65 F.3d 1406 (7th Cir. 1995) (“‘Most favored nations’ clauses are standard devices by which buyers try to bargain for low prices, by getting the seller to agree to treat them as favorably as any of the other customers. The Clinic did this to minimize the cost of these physicians to it, and that is the sort of conduct that the antitrust laws seek to encourage.”). Nevertheless, such agreements could be challenged in certain circumstances, such as:

- When used to facilitate horizontal collusion. *See, e.g.*, *United States v. Apple, Inc.*, 791 F.3d 290, 308 (2d Cir. 2015) (Apple and major book publishers engaged in per se unlawful price-fixing through coordinated negotiations and execution of agency model distribution agreements with most favored nation clauses that effectively raised e-book prices and eliminated price competition in the trade e-books market), *cert. denied*, 136 S. Ct. 1376 (2016).
- Where parties with market power obtain such agreements by coercion and harm to competition results. *See, e.g.*, *Starr v. Sony BMG*, 592 F.3d 314, 323 (2d Cir. 2010) (holding that price-fixing conspiracy claim was supported by allegations that joint ventures formed by major record labels representing more than 80% of internet music

sales used similar MFN clauses in their license agreements, which effectively raised prices for downloading music); *United States v. Blue Cross Blue Shield of Mich.*, 809 F. Supp. 2d 665 (E.D. Mich. 2011) (denying motion to dismiss complaint alleging that MFN clauses in insurer’s agreements with more than 70 Michigan hospitals raised competitors’ hospital costs, excluded competitors from several markets and reduced their ability to compete in many markets, and increased costs to self-insured employers and health insurance prices to consumers, without lowering insurer’s own hospital costs).

- Where the agreement may fall within the scope of state law prohibitions against RPM, i.e., the supplier agrees with a reseller that its resale price of the supplier’s products must be similar or lower than the price at which that reseller sells a competitor’s product (or the same product on a different platform); or
- Where the buyer is entitled to *lower* prices than those granted to other buyers, possibly resulting in price discrimination in violation of the Robinson-Patman Act.

Any proposed agreement in which one or more these red flags is present should be reviewed by counsel.

VI. OTHER VERTICAL RESTRAINTS

1. Exclusive Dealing

Exclusive dealing arrangements include agreements granting exclusive distribution rights, exclusive supply agreements, and restrictions against buying and distributing products manufactured by supplier’s competitors. Loyalty incentives (e.g., discounts or rebates) that encourage customers to buy all or a large percentage of their supply from the supplier offering the incentives may result in *de facto* exclusive dealing arrangements.

Exclusive dealing arrangements frequently provide procompetitive benefits, but they may violate the Sherman Act when they result in substantial foreclosure of competition in the relevant market. While foreclosure is central to determining the competitive effects of exclusive dealing, foreclosure at the distribution level is usually of less concern than foreclosure at the consumer level. *Ryko Mfg. Co. v. Eden Servs.*, 823 F.2d 1215, 1235 (8th Cir. 1987) (“Where the exclusive dealing restraint operates at the distributor level, rather than at the consumer level, we require a higher standard of proof of ‘substantial foreclosure.’”).

With this in mind, proposed exclusive dealing arrangements should be reviewed by antitrust counsel in the following circumstances:

- The exclusive dealing arrangement will aid one of the parties to achieve or maintain market power;
- The term of the arrangement is long (e.g., in excess of 5 years, although what constitutes a long-term agreement may vary by industry), and there are disproportionately harsh economic penalties for early termination that effectively prevent customers from switching to competitors;
- Incentives are significant, available over a prolonged period of time, and designed to deter or even coerce buyers from dealing with the defendant’s competitors. *See, e.g., ZF Meritor LLC v. Eaton Corp.*, 696 F.3d 254 (3d Cir. 2012) (ruling that agreements

containing substantial discounts tied to market-penetration and purchasing targets, which effectively locked competitor out of the market, were unreasonable), *cert. denied*, 133 U.S. 2025 (2013); *Masimo Corp. v. Tyco Healthcare Group L.P.*, 2009 WL 3451725 (9th Cir. 2009) (upholding liability verdict that substantial market foreclosure was due to defendant’s 90 percent market share requirement for loyalty discounts).

2. Territorial and Customer Sales Restrictions

Territorial restrictions prevent distributors and dealers from reselling the supplier’s products outside a defined geographic area. Customer restrictions limit the customers or categories of customers to whom dealers or distributors may sell, including reservation of certain accounts for direct sales by the supplier, such as government sales or national accounts. Under U.S. antitrust law, vertical territorial and customer restrictions generally raise few antitrust concerns unless they result in substantial harm to interbrand competition. As a practical matter, if the supplier imposing the restriction lacks market power, it is unlikely that the restriction will have the requisite adverse effect on interbrand competition. *Graphic Prod. Distribs., Inc. v. ITEK Corp.*, 717 F.2d 1560, 1578 (11th Cir. 1983) (ruling that territorial restrictions imposed by supplier with dominant market share were unreasonable absent evidence that the restrictions worked to address free riding and ensure improved service).

There is considerable divergence between the U.S. and the EU where territorial and customer restrictions are concerned. Article 4(b) of the Block Exemption Regulations provides that restrictions on distributors that entail “market partitioning by territory or by customer group” are hardcore restrictions. Subject to four identified exceptions¹, a supplier may not impose restrictions related to the territory into which or the customers to whom a reseller (i.e., a “buyer”) may resell the supplier’s goods or services.

In 2019, the European Commission fined Japanese company Sanrio Co. Ltd. —the licensor of Hello Kitty[®] merchandise—€6.2 million (\$6.95 million) for prohibiting out-of-territory online sales by licensees, requiring them to refer orders for out-of-territory sales to Sanrio, and imposing other sales and marketing restrictions. Sanrio enforced these restrictions by carrying out audits and punishing noncompliance with nonrenewal. The fine would have been much larger had Sanrio not cooperated fully in the investigations and immediately ceased engaging in the challenged practices.

The distinction between “active” and “passive” sales is important to understanding the extent to which the EU rules protect agreements granting exclusive territories or customer groups. Under

1. The four specifically permitted practices listed in the Block Exemption Regulation, art. 4(b), include the following:

- (i) the restriction of active sales into the exclusive territory or to an exclusive customer group reserved to the supplier or allocated by the supplier to another buyer, where such a restriction does not limit sales by the customers of the buyer,
- (ii) the restriction of sales to end users by a buyer operating at the wholesale level of trade,
- (iii) the restriction of sales by the members of a selective distribution system to unauthorized distributors within the territory reserved by the supplier to operate that system, and
- (iv) the restriction of the buyer’s ability to sell components, supplied for the purposes of incorporation, to customers who would use them to manufacture the same type of goods as those produced by the supplier.

the Guidelines, “active” selling includes soliciting individual customers by direct mail, unsolicited e-mails, or visits, soliciting a specific customer group or customers in a specific territory through advertisements, via the internet or by other promotional activities specifically targeted to that customer group or territory. “Passive” selling refers to responding to unsolicited requests from individual customers and general advertising directed to customers in the distributor’s own territory that incidentally reaches customers in another distributor’s exclusive territory or customer group would also be considered passive sales activity. Within a selective distribution system dealers must be free to sell, both actively and passively, to all end users. It is a hardcore restriction to prohibit retailers in a selective distribution system² from making active or passive sales to end users.

Another hardcore restriction, set forth in Article 4(d) of the Block Exemption Regulation, is the prohibition of cross-supplies between distributors within a selective distribution system, including between distributors operating at different levels of trade. Selected distributors must be free to purchase the supplier’s products from other appointed distributors within the network and may not be forced to purchase the contract products exclusively from a given source. Moreover, within a selective distribution network appointed wholesalers may not be subject to sales restrictions limiting the sales they may make to appointed retailers.

Under Article 4(e) of the Block Exemption Regulations, an agreement between a manufacturer of spare parts and an original equipment manufacturer (OEM), that incorporates those parts into its own products, may not, either directly or indirectly, prevent or restrict sales by the manufacturer of these spare parts to end users, independent repairers, or service providers. An OEM may nevertheless require its own repair and service network to buy spare parts from it.

In the case of a vertical restraint that is neither a hardcore restriction nor within the scope of an identified exception or safe harbor provided by the Block Exemption Regulation, the ordinary EU competition rules apply, and there is no presumption of legality or illegality. The assessment of these vertical agreements requires analysis of whether they are likely to have appreciable negative effects on prices, output, innovation, or the variety or quality of goods and services in the relevant market. Appreciable anticompetitive effects are likely to occur when at least one of the parties to the restraint has or obtains some degree of market power and the agreement contributes to the creation, maintenance or strengthening of that market power or allows the parties to exploit such market power.

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This article is written for educational purposes only and does not constitute legal advice. Always consult with qualified antitrust counsel regarding specific situations and applicable law.

2. “A ‘selective distribution system’ means a distribution system where the supplier undertakes to sell the contract goods or services, either directly or indirectly, only to distributors selected on the basis of specified criteria and where these distributors undertake not to sell such goods or services to unauthorised distributors within the territory reserved by the supplier to operate that system” Block Exemption Regulation, art. 1(1)(e).