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## A Tale of Two Marks, and Other Antitrust concerns

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# A Tale of Two Marks, And Other Antitrust Concerns

By Pamela Jones Harbour\*

## I. Introduction

Having practiced antitrust law for almost twenty years, I believe I am qualified to make the following observation: this is an interesting time in antitrust. The law is evolving in ways I could not have envisioned when I first entered the field.

For example, five Justices of the Supreme Court recently decided in *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*<sup>1</sup> to abandon the vertical restraints dichotomy the Court created thirty years ago in *Continental T.V., Inc. v. GTE Sylvania, Inc.*<sup>2</sup> In *Sylvania*, the Court adopted an extremely familiar, and very important, distinction between price and non-price vertical restraints.<sup>3</sup> For as

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\* Commissioner, Federal Trade Commission. This article is adapted from Commissioner Harbour's remarks at the 7th Annual Antitrust Colloquium at the Institute for Consumer Antitrust Studies at Loyola University Chicago School of Law on April 13, 2007. I would like to thank Prof. Spencer Weber Waller for inviting me to participate in the Colloquium.

<sup>1</sup> *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 127 S. Ct. 2705 (2007).

<sup>2</sup> *Cont'l T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977).

<sup>3</sup> A vertical restraint of trade refers to an agreement or arrangement between actors at different levels of the distribution system. An agreement between a manufacturer and a retailer would, for instance, be a vertical agreement. A vertical pricing agreement typically would involve an agreement between a manufacturer and a retailer regarding the price at which the retailer would resell the goods of the manufacturer to consumers. If such a vertical price fixing agreement required the retailer to sell goods only at or above a price specified by the manufacturer, it would be a vertical minimum price fixing agreement. Thomas K. McCaw, *Competition and "Fair Trade": History and Theory*, 16 RES. IN ECON. THEORY

long as I have been practicing law— at least, until now—vertical price restraints have been *per se* unlawful, while non-price vertical restraints were judged under the rule of reason.<sup>4</sup> But in the wake of Justice Kennedy’s *Leegin* opinion, the distinction between price and non-price vertical restraints no longer matters. Now, *all* vertical restraints are to be judged under the rule of reason.

Members of the US antitrust legal community packed the Supreme Court gallery during oral argument in the *Leegin* case. Many were intensely interested in whether the Court would uphold *per se* illegality of vertical minimum price fixing. The Justices and the parties vigorously debated the merits and demerits of the policy. The very existence of that debate gave me some slight hope that vertical minimum price fixing would remain presumptively illegal. But even then I doubted that the Court would reach a consumer-friendly result.

The *Leegin* outcome is distressing, to put it mildly. I have spent most of my career, in both state and federal government, as an advocate for consumers above all else. Unlike the *Leegin* majority, I maintain that the price/non-price distinction still matters a great

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185, 185 (1996). So-called non-price vertical restraints generally involve the area within which or customers to whom a retailer may sell a manufacturer’s goods. Each type of vertical restraint may increase prices to consumers; however, minimum pricing restraints raise prices directly and non-price restraints may do so, if at all, only indirectly. The Supreme Court in *Sylvania* found that this differential impact, among other things, warranted different legal treatment for price- and non-price vertical restraints. *Sylvania*, 433 U.S. at 51 n.18.

<sup>4</sup> “[T]here are certain agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use.” *N. Pac. Ry. Co. v. United States*, 356 U.S. 1, 5 (1958). Such agreements and practices are said to be *per se* unlawful. Antitrust liability under the rule of reason requires a far more extensive inquiry. “The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts. This is not because a good intention will save an otherwise objectionable regulation or the reverse; but because knowledge of intent may help the court to interpret facts and to predict consequences.” *Chi. Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918). The rule of reason, thus, asks whether the restraint on balance actually harms competition more than it promotes it.

deal—to Congress, to business investors, to many law enforcement officials, and to every bargain-conscious consumer in America. The Court dismantled important consumer protections in *Leegin*. I find myself unable to gracefully accept that and move on. The issues simply are too important to this country.

It is probably obvious by now that I am expressing my own personal views, and not those of the Federal Trade Commission (FTC) or any other Commissioner. This article will begin by looking at insights from “Two Marks” to highlight the difference between things we believe to be true as opposed to those we can prove to be so. The article will then explore the works of economist Robert Steiner to show how the insights of these Two Marks, if ignored, can distort economic models, as well as any rules of law that may rely on those models. The article will next describe the basis for my skepticism regarding the wisdom of the Court’s resolution of *Leegin*. At the end of the article I will offer a remedial prescription for the harm the Court has inflicted on American consumers with its *Leegin* decision

## II. The Two Marks

So, who are the two Marks?

### A. Mark Twain

The first Mark is Mark Twain. We all know about him. Growing up, we were introduced to Tom, Huck, jumping frogs, and an extensive inventory of Twain’s colorful sayings. I am indebted to my friend and former colleague, Michael Salinger (until recently the Director of the FTC’s Bureau of Economics), for sharing the Mark Twain quote<sup>5</sup> I want to highlight. Twain’s statement: “It ain’t what you don’t know that gets you into trouble. It’s what you know for sure that just ain’t so.”<sup>6</sup>

Keep that quote in mind as I relate the following fact: it has been twenty-three years since the Court affirmed a judgment on the

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<sup>5</sup> Michael A. Salinger, Assessing Whether What We Know is So, Address at the American Bar Association 54<sup>th</sup> Antitrust Law Spring Meeting, at 1 (Mar. 31, 2006), available at <http://www.ftc.gov/speeches/salinger/060331ABABreakfastwiththeBureauDirectors.pdf> (last visited Oct. 6, 2007).

<sup>6</sup> Brainyquote.com, Mark Twain Quotes, available at [http://www.brainyquote.com/quotes/authors/m/mark\\_twain.html](http://www.brainyquote.com/quotes/authors/m/mark_twain.html) (last visited Oct. 9, 2007).

merits for a private antitrust plaintiff in a vertical price fixing case. That case was *Monsanto Co. v. Spray-Rite Service Co.*<sup>7</sup> Even here, the Court's language leads most commentators to treat the case as if the defendant had won.<sup>8</sup> The Court engaged in "unidimensional economic analysis," which inflated the likely procompetitive benefits of vertical price fixing with the assumption "that competition at the retail level is either unimportant or will flow naturally from interbrand competition at the producer level."<sup>9</sup>

Many antitrust scholars and practitioners have criticized the Warren Court for creating unacceptable levels of unpredictability in antitrust enforcement.<sup>10</sup> This criticism, indeed, helped spawn the past generation of pro-defendant antitrust holdings. I agree that the proper antidote was to incorporate rigorous economic thinking into antitrust analysis. I worry, however, that the pendulum has swung too far the other way based on mistaken assumptions regarding likely market outcomes.<sup>11</sup>

The basic inquiry of economics is to establish what is true on average. But identifying the average result may not always be good enough to ensure consumer-friendly outcomes—or, at least, outcomes that consumers on average would favor. We need to address a fundamental question: when economists create their predictive models, do their assumptions adequately reflect marketplace realities? And if they do not, do courts that rely on those predictive models do more harm than good to the economy? With

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<sup>7</sup> *Monsanto Co. v. Spray-Rite Serv. Co.*, 465 U.S. 752, 768 (1984). Overall, it has been 22 years since the Court affirmed *any* antitrust judgment on the merits for a private plaintiff. See *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 611 (1985).

<sup>8</sup> See, e.g., LAWRENCE A. SULLIVAN & WARREN S. GRIMES, *THE LAW OF ANTITRUST: AN INTEGRATED HANDBOOK* § 7.1a at 372 (2d ed. 2006) ("The decisions of the 1980s also made the conspiracy requirements for applying Section 1 of the Sherman Act to vertical restraints more rigorous than it had previously been. Decisions such as *Monsanto* . . . appear to use that requirement as a surrogate for substantive policy limits on the law's reach and as a vehicle for enhancing defendants' prospects for obtaining summary judgment on such claims.").

<sup>9</sup> *Id.* § 7.4 at 394.

<sup>10</sup> See, e.g., ERNEST GELLHORN ET AL., *ANTITRUST LAW AND ECONOMICS IN A NUTSHELL* 240-41 (5th ed. 2004).

<sup>11</sup> See *infra* note 21.

respect to economic models of vertical restraints, the polite answer to both of those questions is: we really do not know.<sup>12</sup>

Almost every major antitrust case these days seems to involve dueling economists. Each side of the case often presents one or more eminently qualified expert economists who presumably analyzes the same basic set of facts and data. Yet the experts often reach very different outcomes. They frequently offer conflicting opinions regarding the competitive effects of the evaluated conduct. It is unclear whether we should be more perplexed if half of those economists are wrong, or if all of them are right.

Hence, my Mark Twain quote, which captures the essence of the expert economist conundrum. Do these experts really “know” what they say they know? And if not, how much does this uncertainty cost U.S. consumers? Moreover, if most economists believe something to be true when “it just ain’t so,” a court relying on those beliefs might well adopt a rule of law that is incapable of achieving the intended results. It might even do more harm than good. That is precisely what the Court did in *Leegin*.

## B. Mark Blaug

Now, turn to the second Mark: Mark Blaug. He is a highly esteemed *emeritus* professor of economics at the University of London. Economist friends tell me that Prof. Blaug is as much a philosopher as he is an economist, and that he has written extensively on the history of economic thought and analysis.

*Challenge: The Magazine of Economic Affairs* published an interview with Prof. Blaug in its May-June 1998 issue.<sup>13</sup> The interview of Prof. Blaug began with a discussion of “falsifiability.” He said, “In confronting a theory, it should be possible to think of evidence that, if found, would falsify the theory or would lead you to abandon the theory.”<sup>14</sup>

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<sup>12</sup> See *Leegin*, 127 S. Ct. at 2737 (Breyer, J., dissenting).

<sup>13</sup> *The Problems with Formalism: Interview with Mark Blaug*, CHALLENGE: THE MAG. OF ECON. AFF. (May-June 1998), available at [http://www.btinternet.com/~pae\\_news/Blaug1.htm](http://www.btinternet.com/~pae_news/Blaug1.htm) (last visited Oct. 6, 2007) [hereinafter *Interview with Mark Blaug*]. The publication’s current editorial board includes four Nobel laureates in economics: Paul A. Samuelson (1970), Kenneth J. Arrow (1972), Robert M. Solow (1987), and Joseph E. Stiglitz (2001).

<sup>14</sup> *Id.*

He went on to observe that if a theory, no matter how strongly believed, cannot be falsified, “then whatever this belief is, it is not science because scientific beliefs, theories, hypotheses, or whatever you want to call them, should be falsifiable at least in principle.”<sup>15</sup>

He noted that mainstream economists preach falsifiability, but they do not practice it.

In other words, when confronted with contrary evidence of some beloved theory, they adjust the theory, or they minimize the evidence. Sometimes they even ignore the evidence. They do not look very hard at contrary evidence, preferring to confirm rather than to look for refuting evidence.<sup>16</sup>

Prof. Blaug advocated a change in the priorities of economists. He criticized the profession for assigning “enormous prestige to any kind of economic theory that is mathematically expressed, but almost none to historical argument or a case study. This is a clever way of marshaling empirical evidence to prove a particular economic theory. That is what is wrong.”<sup>17</sup>

His proposed remedy for the economics profession included “more empiricism, more history, more getting your nose dirty in the data, surveying people, asking opinion, [and] monitoring behavior.”<sup>18</sup>

I am by no means an economist. But here we have a highly regarded member of the profession—someone well within the ranks—criticizing a key aspect of how economists do their jobs. At

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<sup>15</sup> *Id.*

<sup>16</sup> *Id.* Prof. Blaug is not alone in this criticism of the profession. “The material about business behavior that students read about in economics textbooks, and almost all of the new theoretical material developed by mainstream professionals and published in the profession’s leading journals was composed by economists who sat down in some comfortable chair and . . . simply made it up.” Barbara R. Bergman, *Needed: A New Empiricism*, 4 *ECONOMISTS’ VOICE*, Iss. 2, Art. 2, (Mar. 2007), at 1, available at [www.bepress.com/ev/vol4/iss2](http://www.bepress.com/ev/vol4/iss2) (follow hyperlink; download document) (last visited Oct. 6, 2007).

<sup>17</sup> *Interview with Mark Blaug, supra* note 13, at 4.

<sup>18</sup> *Id.* at 5. “But is there any other discipline which leaves it’s [sic] theory littered with masses of elegant hypotheses which are testable against observation, without so testing them? Do we have any testable hypothesis about why economists collectively behave with this lack of regard for scientific method?” David Heigham, *Letter: Why Are Economists So Unscientific?*, 4 *ECONOMISTS’ VOICE*, Iss. 2, Art. 5, (May 2007), at 2, available at [www.bepress.com/ev/vol4/iss2](http://www.bepress.com/ev/vol4/iss2) (follow hyperlink; download document) (last visited Oct. 6, 2007).

the same time, I am urged as an FTC commissioner to place increasing faith in economic theories and analyses. I often am asked to rely on the predictions of economists to resolve outcome-determinative aspects of the FTC's enforcement decisions.

Beliefs are a critical part of what makes us human. Sometimes, beliefs can enhance intelligence. But at other times, beliefs may actually restrict the application of intelligence. We have to be able to distinguish between things we can factually demonstrate, and things we "know" are true only because we believe them or believe in them.

The second Mark understands the difference between the two concepts. Others, I fear, may not. This reality exacerbates my concerns about the current state of antitrust law in general, and my particular concern that the Court majority in *Leegin* neither asked the right questions nor found the right answers.

### III. Robert L. Steiner

Robert Steiner<sup>19</sup> shares my concern that most economic models do not accurately reflect how markets for consumer goods actually operate. Steiner has proposed economic models which

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<sup>19</sup> I greatly enjoyed hearing Mr. Steiner's recent presentation on "The Virtual Equivalence of Horizontal and Vertical Competition." Robert L. Steiner, *The Virtual Equivalence of Horizontal and Vertical Competition – An Analysis of the Sources of Market Power in Consumer Goods Industries*, Speech at the 7th Annual Loyola Antitrust Colloquium (April 13, 2007). In 2004, I participated in an American Antitrust Institute program dedicated to Mr. Steiner's work. This "Steinerfest"—and my preparations for it—reinforced my view that we still know far too little about the real-world effects of vertical restraints. Pamela Jones Harbour, *An Enforcement Perspective on the Works of Robert L. Steiner: Why Retailing and Vertical Relationships Matter*, 49 ANTITRUST BULL. 985, 986 (2004), available at <http://www.ftc.gov/speeches/harbour/050311antitrustbulletin.pdf> (last visited Oct. 6, 2007).

"[T]he challenging questions posed by Steiner are in need of answers. Antitrust economists should rise to the challenge and seek these answers, lest the profession risk pursuing an antitrust enforcement policy that, by default, leaves no role for procompetitive vertical enforcement." Other papers presented at this program were published in the same volume.

That day-long program also strengthened my understanding of current federal enforcement policy regarding vertical restraints. The vertical agenda, or lack thereof, appears to reflect a policy choice based on fear—the fear that something *bad* might happen if vertical restraints are attacked. It does not appear to be based on an informed belief that something *good* will happen if vertical restraints are not challenged.



attempt to provide more accurate predictions of whether particular vertical restraints are likely to benefit or harm consumers. The *Leegin* majority would have profited from a better understanding of Steiner's works.

### A. Distribution Competition

Steiner identifies a form of "competition" between manufacturers and retailers,<sup>20</sup> which economists largely have ignored.<sup>21</sup> Steiner argues that neglecting this area of distribution competition can result in mistaken—and potentially harmful—application of the antitrust laws, particularly in retail-driven consumer goods markets.<sup>22</sup>

Most economic models contain a simplifying assumption: that distribution and retail channels are perfectly competitive. Based on this assumption, distribution is viewed as an undifferentiated pass-through for manufacturing costs, competitive conditions, and the like. Steiner calls this the "single-stage" model.<sup>23</sup> Unfortunately, this model is based largely on untested theories of how distribution works.

In reality, distribution intermediaries and retailers often face imperfect competition.<sup>24</sup> Some distribution players may be able to exercise a degree of market power.<sup>25</sup> This should make sense to anyone who regularly shops in the real world. Surely, one would not

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<sup>20</sup> See *infra* notes 22-23.

<sup>21</sup> See Michael P. Lynch, *Why Economists Are Wrong to Neglect Retailing and How Steiner's Theory Provides an Explanation of Important Regularities*, 49 ANTITRUST BULL. 911, 912 (2004) ("Though Steiner's theory [of vertical competition] provides an explanation for otherwise puzzling empirical regularities, his theory seems to have had little or no effect on the way mergers and vertical restrictions are analyzed by antitrust economists.").

<sup>22</sup> See, e.g., Robert L. Steiner, *The Third Relevant Market*, 45 ANTITRUST BULL. 719 (2000); Robert L. Steiner, *Intrabrand Competition – Stepchild of Antitrust*, 36 ANTITRUST BULL. 155 (1991); Robert L. Steiner, *Nature of Vertical Restraints*, 30 ANTITRUST BULL. 143 (1985).

<sup>23</sup> Robert L. Steiner, *A Dual-Stage View of the Consumer Goods Economy*, 35 J. ECON. ISSUES 27, 27 (2001).

<sup>24</sup> Robert Pitofsky, *In Defense of Discounters: The No-Frills Case for a Per Se Rule Against Vertical Price Fixing*, 71 GEO. L. J. 1487, 1492 n.22 (1983).

<sup>25</sup> *Id.* (citing Lawrence A. Sullivan, *Handbook of the Law of Antitrust*, 379 (1977)).

assume that big-box stores—like Wal-Mart or Target—are perfectly competitive with a mom-and-pop store. Thus, the simplifying assumption in most economic models of distribution—that distribution and retailing are perfectly competitive—is objectively flawed.

Steiner would substitute a “dual-stage” model for the prevailing single-stage model. His model would account for the competitive relationships between manufacturers, distributors, and retailers in consumer goods markets.<sup>26</sup> Steiner’s concept of intrabrand “vertical competition” between manufacturers and retailers is fundamentally at odds with the “Chicago School” approach,<sup>27</sup> which views successive levels of distribution as being fully complementary rather than competitive.<sup>28</sup> Steiner finds empirical support for his vertical competition claims, and he notes that these empirical results would not occur if manufacturers and retailers were, in fact, fully complementary.<sup>29</sup>

## B. Rallying Cry for Economists

As an antitrust practitioner, my primary focus has always been on marketplace realities. For this reason, Steiner’s insights resonate with my intuitions about consumer goods markets, as well as with my past experience as a state enforcement official.

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<sup>26</sup> Steiner, *supra* note 23, at 29-31.

<sup>27</sup> Sullivan & Grimes, *supra* note 8, §1.4 at 9. Many Supreme Court decisions reflect Chicago School analysis without fully embracing it. “Chicago School commentators rely heavily on deductive analysis from standard economic assumptions and generally favor a smaller role for antitrust.” See, e.g., *Leegin*, 127 S. Ct. at 2705; *Sylvania*, 433 U.S. at 36. See also Mark Blaug, *Is Competition Such a Good Thing? Static Efficiency versus Dynamic Efficiency*, 19 REV. INDUS. ORG. 37, 47 (2001) (“The Chicago school does not deny that there is a case for antitrust law but they doubt that it is a strong case because most markets, even in the presence of high concentration ratios, are ‘contestable’ (Bork, 1978). How do we know? We know because [of] the good-approximation assumption: the economy is never far away from its perfectly competitive equilibrium growth path! Believe it or not, that is all there is to the ‘antitrust revolution’ of the Chicago School.”). The “good-approximation assumption” refers to the intuition that observed prices and quantities may be treated as good proxies for long-term equilibrium values. *Id.* at 40.

<sup>28</sup> See, e.g., William F. Baxter, *The Viability of Vertical Restraints Doctrine*, 75 CALIF. L. REV. 933, 937-38 (1987).

<sup>29</sup> Robert L. Steiner, *The Inverse Association Between the Margins of Manufacturers and Retailers*, 8 REV. INDUS. ORG. 717 (1993).

Steiner highlights the failure of current economic models to address distribution channel interaction in vertical restraints analysis.<sup>30</sup> It is both curious and troubling that there is no substantial body of economic literature and scholarship on distribution issues. This inattention is especially difficult to explain at this juncture in the history of antitrust law—a time when principles of economics so strongly influence enforcement decisions and judicial outcomes.<sup>31</sup>

We need economic modelers willing to tackle the complexities of real-world markets. We need something more concrete than untested or untestable assumptions and oversimplifying omissions.

Again, I am not an economist. I will not take a position on where I think the economic debate on these issues will, or should, ultimately come out. But Steiner and others—including myself—worry about possible errors of under-enforcement against vertical restraints.<sup>32</sup> If enforcement decisions are made based on fear of the unknown, the enforcers are very likely to make some costly, wrong decisions. Steiner has identified the potential for harm to consumers, and he has posed tough questions that deserve answers. If, as Steiner claims, economic models of distribution markets are incomplete and inaccurate, they can hardly provide courts and enforcers with an accurate assessment of whether vertical distribution restraints benefit or harm consumers.

At the end of my term as FTC Commissioner, I want to be able to say at least two things: that the Commission lived up to the Hippocratic admonition, “first, do no harm,” and that the Commission had an effective vertical restraints enforcement agenda.

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<sup>30</sup> Robert L. Steiner, *Intrabrand Competition – Stepchild of Antitrust*, 36 ANTITRUST BULL. 155,195-96 (1991) (“Intrabrand competition owes its stepchild status in substantial part to flawed economic models. . . . Manufacturers appear [in these flawed models] to deal directly with consumers or to sell to them through an inert distribution segment that simply adds the bare-bones cost of distribution, including a perfectly competitive rate of return, to factory prices.”).

<sup>31</sup> “Economic discussion, such as the studies the Court relies upon, can help provide answers to these questions, and in doing so, economics can, and should, inform antitrust law. But antitrust law cannot, and should not, precisely replicate economists’ (sometimes conflicting) views.” *Leegin*, 127 S. Ct. at 2729 (Breyer, J., dissenting) (emphasis in original).

<sup>32</sup> See, e.g., William Comanor, *Vertical Price Fixing, Vertical Market Restrictions, and the New Antitrust Policy*, 98 HARV. L. REV. 983 (1985); Warren S. Grimes, *Brand Marketing, Intrabrand Competition, and the Multibrand Retailer: The Antitrust Law of Vertical Restraints*, 64 ANTITRUST L. J. 83 (1995).

I cannot condone a “default” enforcement policy based on deliberate ignorance that would endanger both of these goals. I hope economists, therefore, will rise to this new challenge, and provide well-targeted scholarship and better tools for analysis.

#### IV. *Leegin*: The Future Without *Per Se* Illegality for Vertical Minimum Price Fixing

The *Leegin* case presented the issue of *per se* illegality for resale price maintenance—or, as I prefer to call it, vertical minimum price fixing. In particular, the case highlights the dueling views of state and federal antitrust enforcers.

State enforcers argued in *Leegin* for continued *per se* illegality—a view that, in my judgment, accords with experience and pro-consumer public policy.<sup>33</sup> The Solicitor General, the Department of Justice Antitrust Division, and three of the four other Commissioners of the FTC maintained that a full rule of reason analysis should apply, and that the Court’s 1911 decision in *Dr. Miles Med. Co. v. John D. Park & Sons Co*<sup>34</sup> should be overruled.<sup>35</sup>

I disagreed with the position taken by the FTC in the *Leegin* case. I disagreed so strongly, in fact, that I issued a twenty-page public statement setting forth my views on minimum vertical price fixing and the merits of the *Leegin* case.<sup>36</sup> The statement asked, albeit unsuccessfully, for the Court to reaffirm *Dr. Miles*. I will briefly summarize the main points of the statement.

##### A. Historical Context

To provide some factual background, *Leegin* is a manufacturer of women’s fashion accessories marketed under the Brighton® name. *Leegin* entered into vertical minimum price fixing agreements with downstream retailers, primarily specialty

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<sup>33</sup> Brief for the States As Amici Curiae Supporting Respondent, *Leegin*, 127 S. Ct. 2705 (2007) (No. 06-480), 2007 WL 621651.

<sup>34</sup> *Dr. Miles Med. Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911).

<sup>35</sup> Brief for the United States As Amicus Curiae Supporting Petitioner, *Leegin*, 127 S. Ct. 2705 (2007) (No. 04-480), 2007 WL 173650.

<sup>36</sup> Open Letter from Pamela Jones Harbour, Comm’r, Fed. Trade Comm’n, The Illegality of Vertical Minimum Price Fixing, to the Supreme Court of the United States (Feb. 26, 2007), available at <http://www.ftc.gov/speeches/harbour/070226verticalminimumpricefixing.pdf> (last visited Sept. 18, 2007).

boutiques.<sup>37</sup> Under *Dr. Miles*, these types of agreements were condemned as *per se* illegal price fixing since 1911.<sup>38</sup> *Leegin* asked the Court to reverse *Dr. Miles*<sup>39</sup> and, in effect, legitimize vertical minimum price fixing, even though consumers inevitably would face higher prices as a result.

Looking at the underlying history helps reveal the significance of *Leegin*. When the Great Depression began, *Dr. Miles* was the law of the land. During the Depression, however, Congress authorized the states to conduct “natural experiments” in vertical minimum price fixing. Congress did so by enacting an antitrust exemption for so-called “fair trade” laws. Adopted by the states, these laws permitted vertical minimum price fixing.<sup>40</sup> Virtually every state eventually adopted some form of fair trade law.

By the mid-1970s, however, consumers had grown dissatisfied with the effects of vertical minimum price fixing. Most states repealed their fair trade laws. In 1975—faced with a stagnant economy and rampant inflation—Congress reviewed the decades-long natural experiment and deemed it a failure. For the express purpose of providing lower prices to consumers, Congress adopted the Consumer Goods Pricing Act of 1975,<sup>41</sup> which repealed the earlier antitrust exemption for vertical minimum price fixing.

Congress found that vertical minimum price fixing had increased prices to consumers by as much as thirty-seven percent, reduced innovation and efficiency in distribution and retailing, increased the rate of business failures as much as fifty-five percent, reduced entry opportunities for new competitors and products, systematically lowered sales levels per outlet, and diminished the level of both *intra-* and *inter-brand* competition.<sup>42</sup>

Congress considered—and rejected—several justifications for vertical minimum price fixing. These justifications should sound familiar, because they are the same ones often heard today: the promotion of small businesses; the provision of added services; and

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<sup>37</sup> See Petition for a Writ of Certiorari, *Leegin*, 127 S. Ct. 2705 app. D (2007) (No. 06-480), (expert report of Professor Kenneth Elzinga).

<sup>38</sup> *Dr. Miles*, 220 U.S. at 400-01.

<sup>39</sup> *Leegin*, 127 S. Ct. at 2712.

<sup>40</sup> Miller-Tydings Fair Trade Act, Pub. L. No. 75-314, 50 Stat. 693 (1937); McGuire Bill, Pub. L. No. 82-542, 66 Stat. 631 (1852).

<sup>41</sup> Consumer Goods Pricing Act of 1975, Pub. L. No. 94-145, 89 Stat. 801.

<sup>42</sup> See H. R. REP. NO. 94-341(1975); S. REP. NO. 94-466, at 2-3 (1975).

the prevention of free-riding.<sup>43</sup> I find this history compelling. I see no reason to undo what Congress so deliberately set forth back in 1975, especially in the absence of new economic information.<sup>44</sup>

## B. Modern Realities

At least a few modern economists and antitrust scholars agree. Prof. Warren Grimes at Southwestern Law School, among others, has pointed to problems resulting from allowing manufacturers to compete for retailer loyalty by artificially enhancing margins via higher consumer prices. This practice, according to Prof. Grimes, is akin to providing retailers with a consumer-funded bribe. Prof. Grimes argues that this form of commercial bribery is indistinguishable from any other in terms of the potential harm to competition.<sup>45</sup>

In addition, Prof. Grimes notes that if retail margins are enhanced at consumers' expense, a multi-product retailer will have a perverse, and undisclosed, incentive to steer consumers toward particular products. The retailer will do so, even if those products are not the best "match" in terms of price, features, and value.<sup>46</sup> How this incentive to push certain products benefits consumers is beyond me. Nor do I understand how higher prices or margins, by themselves, will incentivize retailers to provide any enhanced services to consumers, and certainly not in some precise mix desired by a manufacturer.

I found unpersuasive the *Leegin* majority's reliance on the concept of "free-riding" as a justification for abandoning the rule of *per se* illegality.<sup>47</sup> I am skeptical that the avoidance of free-riding justifies vertical minimum price fixing, except under rare and narrow circumstances. Professor William S. Comanor and Frederic M. Scherer shared this view with the Court; their amicus brief in *Leegin* stated "there is skepticism in the economic literature about how often

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<sup>43</sup> S. REP. NO. 94-466, at 2-3 (1975).

<sup>44</sup> See *Leegin*, 127 S. Ct. at 2732 (Breyer, J., dissenting) (stating "[w]hat is remarkable about the majority's arguments is that *nothing* in this respect *is new*." (emphasis in original)).

<sup>45</sup> Grimes, *supra* note 32, at 109-10.

<sup>46</sup> Warren S. Grimes, *Spiff, Polish and Consumer Demand Quality: Vertical Price Restraints Revisited*, 80 CAL. L. REV. 815, 834-35 (1992).

<sup>47</sup> See *Leegin*, 127 S. Ct. at 2717.

[free-riding] occurs.”<sup>48</sup> The dissenting Justices in *Leegin* also expressed doubts about the free-riding justification for antitrust leniency for vertical minimum price fixing.<sup>49</sup>

During the *Leegin* oral argument, I was pleased to see Justice Breyer confront *Leegin*’s counsel with the fact that none of *Leegin*’s economic arguments in favor of vertical minimum price fixing reflected new scholarship. Indeed, Justice Breyer stated, virtually the same arguments had been set forth in a 1966 treatise on resale price maintenance.<sup>50</sup>

Justice Breyer also questioned whether the Court, or Congress, was better situated to balance the competing benefits and harms to consumers and producers.<sup>51</sup> His questions during oral argument suggested that Congress might be better suited to explore an important question: whether the 1975 repeal of the fair trade laws spurred retail discounting that could be lost if *Dr. Miles* were overruled.<sup>52</sup> Justice Breyer, joined by Justices Stevens, Souter, and Ginsberg, repeated and amplified these concerns in a particularly cogent dissent.

Until someone demonstrates otherwise, the principle should stand: vertical minimum price fixing almost always leads to higher prices for consumers. Presumptive illegality, therefore, represents sound antitrust, economic, and public policy. The Court should have been very reluctant to change a longstanding rule of law in response to theoretical economic assumptions, especially when these assumptions lack rigorous and valid empirical support. It is unrealistic to assume that distribution and retailing are perfectly competitive in the real world. And once such assumptions are abandoned, most existing economic models are likely to fall apart.

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<sup>48</sup> Brief for Comanor and Scherer as Amici Curiae Supporting Neither Party at 6, *Leegin*, 127 S. Ct. 2705 (2007) (No. 06-480), 2007 WL 173679.

<sup>49</sup> *Leegin*, 127 S. Ct. at 2729-30 (Breyer, J., dissenting).

<sup>50</sup> Transcript of Oral Argument at 12-13, *Leegin*, 127 S. Ct. 2705 (2007) (No. 06-480), 2007 WL 967030.

<sup>51</sup> *Id.* at 17-19. “But both Congress and the FTC, unlike courts, are well-equipped to gather empirical evidence outside the context of a single case. As neither has done so, we cannot conclude with confidence that the gains from eliminating the *per se* rule will outweigh the costs.” *Leegin*, 127 S. Ct. at 2737 (Breyer, J., dissenting). Those costs may include putting at risk substantial investments in discount retailing. *Id.* at 2735-36.

<sup>52</sup> *Leegin*, 127 S. Ct. at 2730-31.

These models likely will not be capable of proving that vertical minimum price fixing is, on balance, good for consumers.

I am willing to concede that it makes sense to have a modified *per se* rule, and to allow a respondent to rebut the presumption of illegality. But the respondent should bear the burden of proof, and should be required to introduce sufficient factual evidence to demonstrate why a particular restraint is necessary in a specific market. For example, a restraint might be needed to cure an identifiable market failure that could not be cured by less restrictive means—provided, of course, that the net benefit to consumers would outweigh the presumptive harm.

Prof. Blaug's advice to consider lessons from history would have been beneficial to the Court. Our country has already experimented with vertical minimum price fixing. Congress declared the experiment a failure. If this country is going to experiment once again with vertical minimum price fixing, then only Congress, not the Court, should sanction a repeat of that experiment. Let Leegin—and other manufacturers who would like to engage in resale price maintenance—explain to Congress why the 1975 repeal of the fair trade laws was a mistake.

In July 2007, I appeared before the Antitrust Subcommittee of the Senate Judiciary Committee to talk about *Leegin*.<sup>53</sup> Sen. Herbert Kohl chaired the hearing and seemed sympathetic to my views on vertical minimum price fixing.<sup>54</sup> If my perception were correct, then manufacturers may have a difficult time convincing Congress that minimum vertical price fixing is good for consumers. During my

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<sup>53</sup> Pamela Jones Harbour, Comm'r, Fed. Trade Comm'n, *The Leegin Decision: The End of Consumer Discounts or Good Antitrust Policy?*, Testimony Before the Subcommittee on Antitrust, Competition Policy and Consumer Rights of the Senate Committee on the Judiciary, 110<sup>th</sup> Cong. (July 31, 2007), *available at* <http://www.ftc.gov/speeches/harbour/070731test.pdf> (last visited Oct. 6, 2007).

<sup>54</sup> Senator Herbert Kohl, Subcomm. Chairman, Senate Judiciary Comm., *The Leegin Decision: The End of Consumer Discounts or Good Antitrust Policy?*, Statement Before the Subcommittee on Antitrust, Competition Policy and Consumer Rights of the Senate Committee on the Judiciary, 110<sup>th</sup> Cong. (July 31, 2007), *available at* [http://judiciary.senate.gov/member\\_statement.cfm?id=2893&wit\\_id=470](http://judiciary.senate.gov/member_statement.cfm?id=2893&wit_id=470) (last visited Oct. 6, 2007). "So I know first hand the dangers to competition and discounting of permitting the practice of vertical price fixing.... We will need to carefully examine whether the Supreme Court's abrupt change to the settled antitrust rule forbidding vertical price fixing will threaten today's vibrant competitive retail marketplace and the pocketbooks of consumers, and consider whether legislation will be necessary to protect the continued existence of consumer discounts."



testimony, I offered the following insights on the post-*Leegin* world of retailing:

As a general matter of antitrust law, a person who can “profitably . . . maintain prices above a competitive level for a significant period of time” is said to possess actionable market power. But the *Leegin* majority articulates a more lenient rule-of-reason standard for minimum vertical price fixing. To quote Justice Kennedy’s version of the rule, “pricing effects” are not enough to establish market power; the plaintiff must make “a further showing of anticompetitive conduct.” To my mind, that is a virtual euphemism for *per se* legality, because it will be so difficult for any plaintiff to make out a case. Therefore, absent Congressional action, I envision a post-*Leegin* world where there is no effective check on vertical minimum price fixing. What will this look like to consumers? Well, if you were to walk through a mass merchandiser’s store, you would see thousands of items produced by hundreds of manufacturers. Each of these manufacturers could require retailers to enter express agreements along the lines of, “you must sell my products at these prices.” Manufacturers also would be able to dictate a variety of other aspects of retail sale, such as shelf location, display spacing, and presentation.

- Will the store owner be permitted to make any meaningful decisions?
- Who will really be running the store?
- How will retailers compete to offer consumers the best deal?

Intrabrand and interbrand competition may continue to exist, but only to the extent it benefits manufacturers, not consumers. In short, the American marketplace will no longer be driven by consumer preferences. And this is wrong.<sup>55</sup>

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<sup>55</sup> Harbour, *supra* note 53 (quoting Dep’t of Justice & Fed. Trade Comm’n, 1992 Horizontal Merger Guidelines §0.1, available at <http://www.ftc.gov/bc/docs/horizmer.shtm> (last visited Oct. 6, 2007)).

The post-*Leegin* world will turn retail merchants into mere sales agents for manufacturers. Retailers, however, should be the purchasing agents for consumers, not just the sales agents for manufacturers.<sup>56</sup> I want to see retailers compete by trying to anticipate consumers' preferences, at prices consumers will find attractive. Some retailers may innovate and provide efficiencies that can be passed on to consumers as lower prices. Other retailers may charge higher prices and offer superior service and ambiance. Consumers should be allowed to make choices among these different options, voting with their wallets for the mix of goods, services, and prices they prefer.<sup>57</sup>

## V. Conclusion

Prof. Blaug criticizes economists for essentially ignoring real-world facts. From an antitrust enforcement perspective, this criticism dovetails neatly with Mark Twain's warning that trouble comes from "what you know for sure that just ain't so."

In a 1977 law review article, Prof. Emeritus John Flynn of the University of Utah College of Law noted that some people question whether economics can be a truly objective science, capable of verifying real-world events. He cautioned that so-called "quantitative" testing is not always as accurate as it might seem.

The first step is to measure whatever can be easily measured. This is OK as far as it goes. The second step is to disregard that which can't be measured or give it an arbitrary quantitative value. This is artificial or misleading. The third step is to presume that what can't be measured easily really isn't very important. This is blindness. The

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<sup>56</sup> See Ruth Prince Mack, *Controlling Retailers* 91 (Faculty of Political Sci. of Columbia Univ. ed., Columbia Univ. Press & P. S. King & Son) (1936) "Control of prices in part determined whether the retailer was the 'selling agent for manufacturer' or 'the purchasing agent for the consumer.'"

<sup>57</sup> See H. R. Rep., *supra* note 42, at 5 (quoting FTC Chairman Lewis Engman) ("Simply put the argument assumes an identity between cost and value and thereby begs the question of the competitive marketplace by denying the consumer the right to assign his own value to the intangible asset of trademark or image."); Pitofsky, *supra* note 24, at 1493 ("[A]uthorizing the manufacturer to decide what mix of products and services is desirable, instead of allowing the market to decide that question, is inconsistent with the nation's commitment to a competitive process").

fourth step is to say that what can't be easily measured really doesn't exist. This is suicide.<sup>58</sup>

I am not ready to let *Dr. Miles* rest in peace without a fight. Based on what little has been “measured” thus far, and my own common-sense observations, I truly believe that consumers will be better off if vertical minimum price fixing remains presumptively illegal. Both the majority and the dissent in *Leegin* recognized that there is virtually no empirical support for the theoretical economic models relied upon by the *Leegin* majority.<sup>59</sup> I will accept that I am wrong—if and when economists do the right kind of work to prove vertical minimum price fixing is beneficial. Until then, however, I will resist shifting the risk of harm to the American consumers I am sworn to protect.

Fixing a minimum resale price necessarily raises the prices of goods purchased by consumers. Some economists have propounded theories that, under narrow circumstances, consumers might benefit from those higher prices. According to the *Leegin* majority, consumers should pay those higher prices—without any possibility of a damage recovery—unless or until the consumer can prove the absence of benefit from those higher prices. In other words, all doubts are resolved in favor of the manufacturer who raised the prices.

Consumers, not manufacturers, deserve the benefit of the doubt. In *Leegin*, the Court has proven itself unwilling to protect consumers from higher prices. It is now Congress' turn to remind the Court of the first rule of antitrust law: “[t]he essence of the antitrust laws is to ensure fair price competition in an open market.”<sup>60</sup> In other words, the consumer comes first.

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<sup>58</sup> John J. Flynn, *Antitrust Jurisprudence: A Symposium on the Economic, Political and Social Goals of Antitrust Policy Introduction*, 125 U. PA. L. REV. 1182, 1186 n.9 (1977) (quoting Daniel Yankelovitch).

<sup>59</sup> Compare *Leegin*, 127 S. Ct. at 2717 (stating “although the empirical evidence on the topic is limited . . .”) (Kennedy, J.) with *id.* at 2729 (asking “[h]ow often, for example, will the benefits to which the Court points occur in practice? I can find no economic consensus on this point.”) (Breyer, J., dissenting).

<sup>60</sup> *Reiter v. Sonotone Corp.*, 442 U.S. 330, 342 (1979) (upholding right of individual consumers to sue for treble damages for price fixing overcharges).