

Conference

"Resale price maintenance - an issue for the European agenda?"

12 September 2008, Vienna/Austria

On 12 September 2008, the Austrian Federal Competition Authority (Bundeswettbewerbsbehörde; BWB) hosted an International Conference on Resale Price Maintenance, a one day conference in Vienna bringing together practitioners from regulatory authorities and private practice as well as academics.

This contribution summarises the main discussion points and draws conclusions of the conference.

1. Background and structure of the conference

The conference "Resale price maintenance - an issue for the European agenda?" on 12 September 2008 in Vienna was the first major international conference organised by the BWB. About 120 delegates attended, two-thirds coming from abroad, i.e. from 26 countries including the US, Indonesia, Israel, Russia, Moldavia, Norway, Switzerland and most EU member states. The audience was mainly composed of delegates from competition agencies and law firms, but also of business people and academics.

In the light of recent developments in the US and the forthcoming revision of the EC Block Exemption on Vertical Agreements, the conference offered a great opportunity to exchange views and to learn about the developments in Europe and the US. In their introductory speeches Bernhard Heitzer, President of the Bundeskartellamt, gave an overview about the European and German situation concerning resale price maintenance (RPM) and William Kovacic, Chairman of the FTC, allowed a better understanding of the US situation in general and the Leegin case in particular. In a first Panel national enforcers explained the economic reasoning of RPM and the enforcement practice of their national competition authority. Following, in Panel 2, practitioners and academics analysed possible loopholes as well as alternatives and summed up their experience. The final panel discussed whether there is a need for change in attitude towards RPM.

It should be mentioned that speakers spoke in their personal capacity.

2. Presentations and main discussion points

All slides used at the conference are published on the conference website www.bwb-conference.at. In the following, the main points are summarised:

Bernhard Heitzer, President of the German Bundeskartellamt, gave an excellent overview of the European and German situation concerning RPM: As a hard core restriction listed in Art. 4 of the Block Exemption Regulation on Vertical Restraints an agreement containing a minimum resale price cannot benefit from the block exemption. There is a negative presumption that such an agreement will not fulfil the conditions of Art. 81 (3) EC: It is assumed that RPM will either not have positive effects or that, where efficiencies are likely to result, these will not be passed on to consumers and/or that RPM is not indispensable for creating these efficiencies. However, it is still possible that Art. 81 (3) EC applies to an agreement if the firm in

question comes forward with substantiated claims that the RPM will bring about efficiencies. If the efficiencies outweigh the negative effects and the other conditions of Art. 81 (3) EC, such as the indispensability test, are also fulfilled, the agreement is not prohibited. In case a maximum resale price is imposed on the buyer or where a particular resale price is only recommended, the agreement can benefit from the block exemption. He did not consider Leegin as a starting shot for reforming RPM in Europe. Rather, the methods of treating RPM in the US and Europe may even converge: Both systems now follow a rule of reason approach. The burden of proof on vertical price fixers may be higher in Europe. Due to the differences between European and US markets Heitzer warned against taking up economic thinking adopted with the US economic model in mind. He was very sceptic that inter-brand competition could often outbalance the anticompetitive effects due to the loss of intra-brand competition caused by RPM.

William E. Kovacic, Chairman of the US Federal Trade Commission, provided an excellent insight into the US system and the background of the Leegin decision. He illustrated how the legal rules developed in the Dr. Miles decision in 1911 changed and softened until Leegin. While Dr. Miles forbid minimum resale price maintenance as well as non-price restraints as per se illegal (it was considered to be too complicated to separate the good from the bad), in the Sylvania decision in 1977 non-price restraints were put under the rule of reason. First thoughts arose whether RPM should remain per se illegal, but the time was not ripe yet. In decisions in 1984 and 1988 the term "agreement" was redefined and in the Leegin case in 2007 the Supreme Court finally decided that also minimum resale price maintenance should be evaluated under the rule of reason. Kovacic stressed however, that the decision was a tight one (five to four) and that States do not necessarily go along with the decisions of the Supreme Court. Some states (e.g. New York and California) are strictly against the Leegin decision - therefore "compliance programmes should not be thrown away". In light of the Leegin decision of the Supreme Court, in 2008 the FTC granted a petition by women's shoe company Nine West to modify a prior order prohibiting it from engaging in RPM. Kovacic informed that the FTC will hold a workshop to develop how to go ahead. They will start a research programme and envisage a co-operation with Europe in order to collect necessary empirical evidence on RPM from all jurisdictions.

Panel 1 gave an overview of the (economic) reasoning of the enforcement practice of national competition authorities. It became clear that many competition authorities investigated RPM cases, e.g. the Czech authority is currently focusing on RPM cases, while e.g. the Dutch authority follows a more lenient approach: this is partly due to a decision by Dutch Court that the NMA has to prove appreciable effects of RPM. Many favoured a very cautious approach to RPM as recent literature confirmed that RPM can cause serious harm and efficiency benefits might not be that convincing. In several competition authorities RPM is the most complained about practice.

First, **Anne Perrot**, Vice-President of the Conseil de la Concurrence, explained the economic reasoning of RPM: RPM can avoid double marginalisation, increase inter-brand competition by increasing sales services and can avoid free riding. On the other hand RPM can facilitate upstream collusion, it can help to extract monopoly profits and lead to higher prices. Perrot stressed that many economists consider that

RPM should be evaluated under the rule of reason but that new models predict that RPM is mostly anticompetitive. In France 16 cases were sanctioned since the entry into force of the Block Exemption Regulation. In a case by case analysis three cumulative criteria have to be evaluated: retailer have to be aware of the retail price the supplier wants them to charge; prices are monitored to prevent any deviation by a retailer; and recommended prices are followed by a significant number (80 %) of retailers.

Amelia Fletcher, chief Economist of the Office of Fair Trading, showed that after the removal of RPM for books in 1997 more books were sold and more titles were published while the effect on prices remained unclear: individual prices rose partly, however important discounts were offered and models like "buy three for two" evolved. Furthermore, new entry was enabled by novel distribution channels like supermarkets. This experience might lead to the conclusion that the efficiencies often claimed to become true only by RPM might not be that convincing. Furthermore, Fletcher reported on two object cases concerning toys and football kits. As a conclusion Fletcher stressed that recent literature confirmed that RPM can cause serious harm and efficiency benefits might be overstated, like the experience in the book case showed. This would favour an object approach while leaving the possibility for exemption under Art. 81 (3) EC, subject to indispensability, important. Fletcher concluded that it is important to set out a theory of harm in order to have a good decision basis for setting fines and for case prioritisation - a field the OFT will work on.

Robert Neruda, Vice-Chairman of the Czech Office for the Protection of Competition, reported that in 2007 the Czech competition office took the strategic decision to focus more on RPM and therefore has recently engaged in several investigations of RPM. This was due to the fact that the former lenient approach led to a widespread use of RPM in the Czech Republic. The authority therefore wanted to restore the credibility of enforcement, encouraged by the fact that Czech retail prices seem to be the highest in the region and competition inefficient. Neruda therefore favoured to retain the system of rebuttable presumption of illegality (with the burden of proof of pro-competitive effects on undertakings). Otherwise, legal certainty would be reduced, costs of enforcement would be increased dramatically and strict bans on more serious infringements like horizontal price fixing might possibly be jeopardized.

René Jansen, Member of the Board of the Dutch competition authority, reported that the NMa follows a more lenient approach to RPM. This was partly due to the fact that in 2005 the Trade and Industry Appeals Tribunal, the highest court to rule on competition cases, overturned an NMa-decision regarding RPM. It decided that - although the specific agreement had the objective to restrict competition - the agreement has to have an appreciable effect on the market in order to be prohibited. As the NMa had not investigated this issue, the NMa was ordered to reassess the case. Finally, the NMa dropped the case as the evidence collected pointed into the direction of very low market shares. Now the NMa dismisses most of the claims concerning RPM after a short investigation as most sectors showed very strong inter-brand competition and there was little evidence for the facilitation of horizontal cartels. While there are some cases where competition authorities undoubtedly have to intervene (e.g. when RPM is used to execute market power or to enhance

transparency in a horizontal cartel), the NMa considers it merits discussion whether minimum resale price maintenance should be treated similar to other vertical agreements under the Commission's block exemption for vertical agreements. An interesting proposal of Jansen was to understand the Leegin decision as a natural experiment to detect whether developments after Leegin have more pro- or more anti-competitive effects.

Luc Peeperkorn, Senior Administrator of DG Competition and leading official for the review of the Block Exemption Regulation on Vertical Agreements, stressed that - unlike the former per se prohibition in the US - in Europe there is always room for companies to come forward with substantiated claims that RPM will bring about pro-competitive effects. Many of the cases dealt with under Article 81 in the last 10 years concerned RPM, where the RPM was often applied in combination with other hard core restrictions. In none of these cases the parties came up with convincing efficiencies. It can be expected that in general RPM will neither be an effective nor an indispensable means to create efficiencies. For example, in the discussion it was suggested that RPM could be useful for a manufacturer to provide the right incentives to its distributor in case the latter is also a rival of the manufacturer. Peeperkorn argued that in this case a maximum price and not a fixed or minimum price would be the appropriate measure. Free riding, another often used argument for RPM, can also not be avoided by RPM - it does not effectively provide an incentive to spend the extra profit obtained as a result of the price increase on promotion and services.

Panel 2 considered loopholes and alternatives to RPM and summarised the experience of practitioners.

Patrick Krauskopf, Deputy Director of the Swiss Competition Commission, reported that RPM was abolished three years ago in Switzerland. The intermediate findings, published at the beginning of September, however did not show clear results. This might be due to the fact that time is just too short to produce clear effects.

Andreas Reindl, Executive Director at the Fordham Competition Law Institute, showed that suppliers can use a broad range of restraints and strategies to soften price competition among its retailers while not applying RPM: non-price restraints like exclusive territories, service and promotion obligations; price-related strategies like co-operative advertising programmes including minimum advertising prices or recommended prices; and "no-agreement strategies" focusing on unilateral conduct and the like. Even though "alternative" strategies may serve a similar purpose as explicit RPM and may have the same effect of raising retail price, they are treated much more favourable under the competition law as their pro-competitive rationales are more readily accepted than in cases of explicit RPM. Reindl was concerned that current EU competition law operates in a strict black and white model where a price-related restraint was either blacklisted and therefore "quasi per se" unlawful or would fall under the block exemption and was therefore not subject to any analysis. This situation would focus on the wrong question: the emphasis is mainly put on the characterisation (RPM or not? price or non-price?) rather than on the analysis of the competitive harm. This leads to more legal uncertainty than might be expected. With the trend toward settlements, the room for competition authorities to "hide" weak or unclear cases increases which could further increase legal uncertainty and

undermine predictability. Therefore a better analytical framework should be developed to determine when a case involving price restraints could raise competitive concerns that should be further investigated.

Volker Viechtbauer, Head of the Legal Department of Red Bull, explained that RPM is a clear no-go for Red Bull. It is hard to explain to sales people and to convince them. A strong commitment from the highest management level is a precondition. From Red Bull's business perspective the most important drawbacks of the prohibition of RPM is that it makes parallel trade attractive and leads to a slow margin erosion of the operators. Viechtbauer stressed however that parallel trade is an issue Red Bull accepts and has to accept as a matter of fact. Alternatives to RPM include maximum resale prices or recommended resale prices, however it is rarely used with Red Bull. Further alternatives comprise price corridors at the international level (this is however hopeless in case of exchange rate variations), the differentiation of goods and services as well as the choice of the right distribution channels.

Felix Michael Klement, Partner at the law firm Wildmoser, Koch & Partner, considered that the application of Art 81 (3) EC seems to be impossible in most cases of RPM, particularly as the fair share for consumers is difficult to substantiate: neither the additional value of increased services nor of a market entry can be quantified. He criticised the lack of guidance for the assessment of RPM under Art 81 (3) EC. Furthermore, Klement deemed it incomprehensible that - while a price recommendation is allowed - a not enforced compliance with the recommendation might be considered a cartel.

David G. Anderson, Partner at the law firm Berwin Leighton Paisner LLP, reported that - when discussing about Leegin - he was confronted with the statement that "the difference between the permitted and the prohibited is understood only by lawyers and people from mars." Being US national but advising also clients in Europe for more than 15 years, he compared EU and US practice. He concluded that the EU has historically been more hostile to vertical restraints than the US. Even when RPM was per se illegal in the US, loopholes existed with the Colgate decision already for decades. However, in Anderson's experience Leegin did not yet trigger much public debate in Europe - except at this conference. He thought that a serious discussion about RPM is however needed and criticised that - as RPM is largely a no-go in the EU - it is impossible to collect experience what would really happen. He proposed to evaluate RPM in the future at least under the concept of appreciability or the de minimis rule: if market shares are low, concerns regarding prices and collusion are low, too.

Finally, **Panel 3** discussed whether there is a need for change in Europe and if yes, in which direction this should go.

Luc Peepkorn, Senior Administrator of DG Competition and leading official for the review of the Block Exemption Regulation on Vertical Agreements, stressed that due to the difference between the US per se approach (no efficiency defence at all possible) and the EU hardcore approach (efficiency defence not excluded) the potential need for change is not the same in the EU as it was in the US. In the US the question how RPM should be assessed still needs to be answered - a question that will be reconsidered also in the EU in the course of the review of the vertical

restraints regime. The answer how to assess RPM will depend on the likelihood of both its negative and its positive effects. Peeperkorn was sceptic that all efficiencies linked in general to vertical restraints can also be realised effectively through RPM. He was not convinced of the argument brought forward at this conference that the burden of proof under Art. 81 (3) EC for RPM is too difficult to overcome as this would then be true for all agreements. The current EU approach therefore might be a good option also for the future, although it certainly merits more discussion.

Luc Gyselen, Partner at the law firm Arnold & Porter LLP, stressed that the burden of proof under Art. 81 (3) EC is allocated in a different manner than under the US rule of reason making it much more difficult for companies in the EU. He criticised that in the EU no analysis of the market power takes place when assessing RPM. Furthermore, as RPM is a hard core restriction listed in Art. 4 of the Vertical Block Exemption Regulation (BER), the whole agreement falls outside the scope of the BER. A classification under Art. 5 of the BER (making only the specific provision not to benefit from the BER) would already help. In general however, he hoped that in the future pro- and anticompetitive effects of RPM will be assessed as is done with other vertical restraints or Art. 82.

László Szakadát, Member of the Hungarian Competition Council, was even more pronounced and argued that RPM should in general be lawful unless the competition authority has evidence for the existence of anti-competitive effects. RPM should only be challenged if it is a facilitating device of the company to monopolize or to collude. The burden of proof should be on the competition authority. Szakadát proposed to set up certain safe harbours.

Konrad Ost, Head of Unit for German and European Competition Law in the Bundeskartellamt, warned on the administrative burden if RPM would be qualified as basically harmless and actual anticompetitive effects would have to be proven by the competition authority: Watering down RPM rules would make enforcement unreasonably cumbersome and ineffective in practice. In reality, a kind of rebuttable presumption in favour of RPM legality would thus mean giving "carte blanche" to potential abusers. This would not be justified due to the low likelihood of pro-competitive effects: there is only a vague expectation that there might be cases which might prove to be pro-competitive.

As moderator of panel 3 **William E. Kovacic**, Chairman of the Federal Trade Commission, summarised the thoughts discussed: As everything depends on a presumption of efficiencies and the likelihood of pro-competitive effects of RPM, more economic/empirical work should be done. As budgets of national competition authorities are low, it could be envisaged to co-operate with universities. Furthermore, the introduction of some kind of analysis of market share/de minimis could be thought of in order to check whether potential negative effects are likely. (Also in Leegin and in Nine West market shares were very low.)

Theodor Thanner, Director General of the Austrian Competition Authority, finally summarised the main discussion points and drew conclusions.

3. Conclusions

As - at least for several competition authorities - RPM seems to be the most complained about practice, a change in attitude towards RPM might entail important consequences for competition authorities. While - due to the recent legal status of RPM - consequences of RPM could not yet be studied in practice, Leegin might be seen as natural experiment. The US FTC will hold a workshop and start a research programme in order to define how to assess RPM. Also in Europe there is the feeling that - at least for case prioritisation - some more research/deliberations would be needed.

Several competition authorities expressed the fear of a too high administrative burden in case of a more lenient approach to RPM in the light of an unclear probability of pro-competitive effects. The UK's experience concerning the abolishment of RPM in book retailing points into the direction that claimed efficiencies might be overstated. Some raised doubts that the objectives claimed to be followed by RPM are really efficiently achieved by minimum resale prices. Most of the competition authorities seem to favour the current approach, while some other competition authorities as well as lawyers and academics would support to treat minimum resale price maintenance similar to other vertical agreements. In this way a black and white model could be avoided and the emphasis could be mainly put on the analysis of the competitive harm rather than on the characterisation (RPM or not? price or non-price?).

While still differing in opinion, it seemed that a common understanding could be reached that the introduction of some kind of analysis of the market share/appreciability might at least merit further discussion. Due to a Court decision the Dutch competition authority already has to analyse whether the RPM agreement has an appreciable effect on the market. Also in the US further developments have to be pursued as at the moment some Federal States which do not necessarily have to follow the Supreme Court seem to be unwilling to follow the Leegin decision.

To summarise, pros and cons were put on the table. Thereby the conference achieved its aim to form a good basis for discussion in the European Union on the review of the Vertical Block Exemption Regulation.