

# **Resale Price Maintenance: A Historical View of Its Impact on the Sporting Goods Industry**

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## **■ INTRODUCTION**

Resale price maintenance (RPM) is a system in which the manufacturer of a branded or trademarked product dictates the resale price for the products it sells within the chain of distribution. The practice itself constitutes a vertical restraint of trade since RPM dictates the price at which competing sellers sell a product. Many argue that the vertical pricing restraint represents an agreement, contract, or conspiracy to restrain trade in violation of section 1 of the Sherman Act (15 U.S.C. § 1). For this reason, the manufacturer's ability to engage in RPM practices has fluctuated over the years as the courts and Congress have vacillated over its legality.

Sporting goods manufacturers have been concerned about resale price maintenance since the late 1800s. Early RPM advocates included Spalding, A. J. Reach; J. Stevens Arms & Tool Co.; Marlin Firearms Company; Colt; Savage; and Harrington & Richardson (West, 1904). During the 1890s the bicycle industry experienced tremendous growth and competition. When the popularity of the bicycle waned in the late 1890s, competition became even more intense. The bicycle crash which followed forced many companies into bankruptcy. Much of the sporting goods industry concern regarding price control emanated as a result of the bicycle crash in 1899. In the aftermath of the bicycle crash (1899-1900), some manufacturers pointed to the price-cutting tactics of the catalogue and mail order houses as a significant cause of business failure. Sporting goods manufacturers concerned about business profits and industry profitability considered RPM an integral business strategy influencing long-term success. In response to restraint of trade claims, manufacturers advocating RPM practices argue that RPM has many pro-competitive effects which outweigh the pricing restraint imposed upon the distributor.

This article begins with a discussion of the benefits of RPM from the point of view of the sporting goods manufacturers. It then traces the judicial and legislative history that influences RPM practices in the sporting goods industry. In conclusion, the article comments on the present position of RPM and alternate ways in which sporting goods manufacturers can legally maintain resale prices.

## ■ MANUFACTURER BENEFITS ASSOCIATED WITH RPM PRACTICES

### 1. Eliminates loss leader tactics

RPM prohibits distributors from promoting a manufacturer's product as a loss leader. Loss leading selling is a competitive strategy in which brand name, highly advertised, and high demand products are sold by distributors at a loss (i.e., below cost). The perceived value associated with purchasing branded, highly advertised, and high demand products at a discount "leads" many consumers to the particular distribution outlet. Sporting goods manufacturers look with disfavor on retailers using their products as loss leaders for three reasons.

First, as argued by the sporting goods industry, loss leading is an unethical practice which exploits the consumer. As explained by Bowman (1955), consumers are drawn into a store to purchase the discounted, brand name product. However, retailers engaged in loss leading tactics discount the attractive, high demand products as a way to deceive consumers into thinking that all products carried by the distributor are offered at discount prices. Once in the store, consumers purchase additional items with the assumption that the distributor has priced all items at favorable prices. Contrary to public perception, distributors typically sell non-loss leader items at high margins to enable the distributor to recoup losses associated with selling brand name products at extremely low margins or below break-even values. Consequently, the consumer typically is deceived into paying exorbitant prices for inferior goods.

Second, small scale, specialty sporting goods retailers are often unable to compete with distributors engaging in loss leading tactics. Unlike the discount house or chain store, the small, specialty retail stores typically do not carry an extensive product mix or large inventory. Consequently, there is not the product diversity necessary to enable the small sporting goods retailer to earn a profit on non-loss leader items. In response to loss leading tactics, small specialty stores followed one of two options. Either the small specialty dealers ceased to carry products which competing dealers sold as loss leaders or they liquidated their retail operation. Dealers forced to discontinue carrying products used as loss leaders instead sold substitute, private label and imported items at comparable prices. Small specialty distributors unable to engage in loss leading tactics and unable to secure a market for comparable private label items were frequently forced to liquidate operations (Yamey, 1966; "Some Views," 1906). The severity of this problem is represented in Procknor's data.

As noted by Procknor, in 1933 there were between 1500 to 2000 business failures per month. Small specialty sporting goods retailers criticized the sporting good manufacturer who did not adhere to RPM practices. The criticism began when the small, specialty sporting goods retailer encountered competition from the mail order houses in the early 1920s and peaked in the 1960s when the retailers encountered competition from discount houses, PXs (i.e., government owned and operated stores), chain stores, and department stores. Failure to engage in prudent business practices, such as supporting RPM, was cited as the number one reason for

business failures (“We Need Help Badly,” 1960). Regardless of the option pursued, manufacturers of the loss leader products lost the business of the small distributors. Further, their products lost retail visibility and remained unavailable to the consumers frequenting the specialty sporting goods store (Arquit, 1992).

Third, manufacturers disfavor distributors selling their brand name products as loss leaders because loss leading tactics often dilute the investment a company has made toward the establishment of a reputable brand image associated with product quality (Arquit, 1992; Yamey, 1966). Robert B. Dunlap, concerned about the sale of Dunlap golf balls by price cutters and mail order houses, explained the matter to readers of the *Sporting Goods Dealer* in 1912. As explained by Dunlap,

The manufacturer’s distribution, which it has taken months or years and often hundreds of thousands of dollars to establish, is entirely demoralized and the good will of the legitimate jobbers and dealers, whom his advertising has induced to stock his goods, is lost beyond recovery (Dunlap, 1912, p. 30).

The association between quality and price is further explained by Congresswoman Nolan in a 1926 article appearing in the *Sporting Goods Dealer*. Congresswoman Nolan states that women shoppers, the individuals buying over 50% of all merchandise, prefer RPM. As Congresswoman Nolan explained,

In the mind of the average woman definite prices and definite qualities are inseparable. When she is accustomed to using the same brand and finds that the price of this brand has suddenly shifted, her first thought is that the quality has changed, too. She loses faith (Congresswoman, 1926, p. 137).

Loss leading sales, and more specifically, discounting sales below reasonable margins, brought havoc to the sporting goods industry. Although loss leading was a continual problem dating back to the late 1800s, the crisis peaked during the late 1920s and again in the late 1950s. The manufacturer, wholesaler, jobber, and retailer all suffered as a result of loss leading practices. Specialty sporting goods retailers, unable to compete with the discount houses engaging in loss leading tactics, blamed manufacturers, wholesalers, and jobbers for breaching established RPM practices and selling directly to the discount houses. In defense, the manufacturers argued that discounters were receiving goods from uncooperative wholesalers and jobbers (Autz, 1957a). J. K. Dougherty, President of the Associated Fishing Tackle Manufacturers, summarized loss leading practices as bad economic business and encouraged distributors to “sell up.” Manufacturers unable to eliminate loss leading sales turned to Congress for assistance. By 1966, 31 states had statutes prohibiting selling below cost. These statutes significantly curtailed the practice of loss leader sales (Jones, 1960; LaRue, 1963).

## **2. Encourages service provisions**

The sporting goods industry recognized the association between service provisions and product sales as early as 1900. Service provisions play an important role in the sale of sporting goods for a number of reasons. For example, the salesperson’s involvement in the organization of teams, leagues, and tournaments provides participation opportunities for customers (“Methods of distribution,” 1908). In addition, demonstrating the correct usage of a product, providing the

consumer with related product literature, providing product installment, and post-sales service all promote proper product usage. Proper product usage has three benefits. First, proper product usage increases the longevity of the product itself and subsequently generates customer satisfaction. Second, proper product usage reduces the product-related accidents and injuries occurring as a result of improper usage. Third, proper product usage enables the consumer to capitalize on the real performance capabilities of the sporting goods product.

RPM requires distributors to compete on service offerings (e.g., a trained sales force, product literature) since intrabrand price competition is eliminated. However, due to the expense associated with service provisions, distributors are often reluctant to offer services unless the manufacturer adheres to a RPM policy. Retailers demand RPM as RPM eliminates the “free riding” phenomenon which occurs when the non-service, discount dealer benefits from the services of full-service dealers (Arquitt, 1992, Goldberg, 1984). For example, a consumer in the market to purchase a bicycle can visit a full-service retailer to gain knowledge and gather literature about bicycle technology, usage, and brand differentiations. It is the practice of the full-service distributor to spend a great deal of time and expense educating the consumer and communicating with this potential patron. Free-riding occurs when this potential patron uses the knowledge gained from the full-service dealer and purchases the final product at a cheaper price from a non-service, discount dealer. As noted by a specialty sporting goods distributor (Autz, 1957b),

The No. 1 gripe of smaller retailers is the use of their stores as “showrooms” for cut-price items . . . . The other day, two fellows walked into my store and looked at some spinning reels, which we mark at the normal retail, \$17.95. After I spent a good hour explaining how the reel worked, demonstrating, etc. one of the fellows turned to me and said: “Thanks. We just wanted to see if these reels were worth \$10.77 as shown on our wholesale catalog” (p. 112).

Other distributors reported similar comments to Autz, the *Sporting Goods Dealer* editor, in 1960 (Autz, 1960). For example, one distributor stated, “We got tired of being a sample room . . . and closed out our entire line of sporting goods” (Autz, 1960, p. 156) Autz (1960) quoted another distributor frustrated with the free riding phenomenon. As explained by the distributor,

We have our own pond where we demonstrate tackle. These people would have the nerve to come back with the tackle they bought elsewhere at a discount and ask us to show them how it works. After helping them out, they’d say they’d be back but we’d never see them again (p. 156).

RPM protects full-service retailers against free-riding by forcing all dealers to sell a manufacturer’s product at a specified price.

### **3. Mitigates buyer power**

Manufacturers also favor RPM as it mitigates buyer power, or the power of the distributor, in two ways. First, retailers are not compelled to negotiate extensively with a manufacturer for low cost purchases since RPM ensures retailers favorable margins and eliminates intrabrand price competition. The elimination of RPM would increase intrabrand price competition and eliminate established margins.

The reduced profit margins of the distributors force them into extensive negotiations regarding the cost of purchases. A writer for the *Sporting Goods Dealer* echoed these sentiments as early as 1910. "Buyers," he said, "like clean-cut buying. Clean-cut buying can only be made possible by the single fixed price on goods, so that all possibility of haggling is done away" ("Value of Fixed Prices," 1910, p. 24). Consequently, manufacturers attempting to avoid reducing their own margins favor RPM. Second, backward integration is an option when frustrations mount between a supplier and buyer. A distributor of sporting goods who integrates into manufacturing would be problematic for existing sporting goods manufacturers as they would simultaneously lose a buyer and gain a competitor. Distributors of sporting goods products which earn favorable margins are less likely to threaten existing manufacturers with vertical integration possibilities.

#### **4. Encourages research and development**

RPM encourages research and development and product innovation in two ways. First, RPM is effective when manufacturers introduce new products which the retailer might be reluctant to promote. Distributors of new sporting goods products are hesitant to carry new products which have no established demand. However, RPM practices which provide a built-in profit margin provide a distributor with a monetary incentive to carry and sell the newly developed products (Bowman, 1955). Second, as noted above, RPM reduces the buyer's inclination to negotiate over the price of supplies purchased from the manufacturer. However, if manufacturers were forced to sell at lower margins, less money would be available to devote toward research and development. Manufacturers, realizing the importance of research and development as it relates to long-term company viability, strongly favor RPM for this reason.

#### **5. Reduces business expenses associated with alternate methods of price control**

RPM, in comparison to alternate methods of price control, is viewed by sporting goods manufacturers as the most attractive price control measure. For example, consignment selling is a legal way to retain control of distribution and prices. However, the sporting goods manufacturers did not favor consignment selling ("Revisions," 1933). Consignment selling, although attractive to the distributor, forces the manufacturer to retain title to the goods and absorb all risk associated with the product. For example, in a legal consignment system, the manufacturer is responsible for paying all taxes (e.g., property, inventory, sales) and absorbing all product losses associated with unsold, damaged, or obsolete goods (Benton and Gross, 1993; Yamey, 1966). Further, the manufacturer does not receive any cash flow until the product is actually purchased by the end user.

Vertical integration is another means available to a manufacturer seeking to control prices. However, similar to consignment selling, this is an expensive alternative to RPM available to only select, capital rich sporting goods manufacturers.

## ■ JUDICIAL AND LEGISLATIVE HISTORY INFLUENCING RPM PRACTICES

### **The Sherman Antitrust Act, 1890**

The Sherman Act of 1890, passed in an era of anti-monopoly sentiment, is designed to promote free and open competition in an environment free of monopolistic tendencies. Section 1 of the Sherman Act prohibits “contracts, combinations, . . . or conspiracies in restraint of trade or commerce among the several States.” RPM, or vertical price fixing, is viewed as a restraint of trade as it precludes distributors and retailers from establishing their own prices at which to sell products in interstate commerce. However, the language within the statute itself does not directly define what constitutes a contract in restraint of trade. Consequently, the judiciary and enacted legislation play paramount roles in the interpretation and application of the antitrust laws regarding RPM or vertical price fixing.

### ***Dr. Miles Medical Co. v. Park & Sons Co. (1911)***

The Supreme Court first addressed the legality of RPM in the seminal case of *Dr. Miles Medical Co. v. Park & Sons Co.* (1911). Dr. Miles Medical Company, an Indiana corporation, manufactured and sold proprietary, non-patented medicines. Dr. Miles established the prices for the entire distribution chain and stipulated with whom the distributors could deal. For example, all distributors were contractually prohibited from selling products to discounters. Dr. Miles Medical Company sued a wholesale drug company actively discounting the prices of Dr. Miles products. Dr. Miles argued that small retailers were no longer willing to carry the proprietary medicines due to their inability to compete on prices. In addition, Dr. Miles was concerned about its diminishing product demand and perceived quality image, reputation, and goodwill of his company. The Supreme Court, much to the surprise of industry, ruled that RPM was a per se violation<sup>0</sup> of the Sherman Act. In addressing the legality of Dr. Miles’ restrictive agreements, Justice Hughes explained,

The public have an interest in every person’s carrying on his trade freely; so has the individual. All interference with individual liberty of action in trading, and all restraints of trade of themselves, if there is nothing more, are contrary to public policy, and therefore void (31 S.Ct. 384).

## ■ THE ERA OF PATENT PROTECTION

### **Post-Miles Assurances**

Regardless of the per se ruling in the Dr. Miles case, articles appearing in the *Sporting Goods Dealer* throughout 1911 assured sporting goods manufacturers that the Dr. Miles decision would not impact current RPM practices within the sport industry. The key distinction, as explained by Mr. Maxwell (Iver Johnson’s Arm & Cycle Company Sales Manager), focused on the non-patented nature of Dr. Miles products, whereas the majority of RPM agreements in the sporting goods industry

involved patented sporting goods products (“The Supreme Court Speaks,” 1911). The patent laws allowed the owner of a patented product to “vend”, or sell, as desired, including the establishment of the product’s resale price (16 Stat. 198; *Bloomer v. McQuewan*, 14 How. 539; *Continental Paper Bag Co. v. Eastern*, 210 U.S. 405). As explained by the Circuit Court of Appeals, Seventh Circuit, in *Rubber Tire Wheel Co. v. Milwaukee Rubber Wheel Co.* (1907), the patent owner’s reward for invention is the absolute security of “making, using, or vending” the patented product as so desired for a period of 17 years. Violations of RPM constituted patent infringement. Further, as explained by the Circuit Court of Appeals, Seventh Circuit, in *Rubber Tire Wheel Co. v. Milwaukee Rubber W. Co.* (1907), patented articles were not subject to antitrust scrutiny. As stated by the court,

Patented articles, unless or until they are released by the owner of the patent from the dominion of his monopoly, are not articles of trade or commerce among the several states (p. 362).

The *Sears, Roebuck & Company v. Iver Johnson’s Arms and Cycle Works* case in 1911 illustrates the patent protection provided to sporting goods manufacturing companies (“Supreme Court Decision,” 1911). Iver Johnson, manufacturer of arms and ammunition, wanted to insure that its new 1910 patented revolver would be sold at prescribed prices. To accomplish this objective the company sold this patented product only through company authorized jobbers. Authorized jobbers were prohibited from selling Iver Johnson’s revolvers to mail order houses. The Chicago mail-order house challenged the legality of the Iver Johnson distributor agreements, claiming that the manufacturer’s refusal to deal constituted a conspiracy with other distributors to enforce RPM. The case, decided by the Supreme Court of Massachusetts, was decided in favor of the patent holder, Iver Johnson.

### ***Henry v. A. B. Dick Company (1912)***

The *Henry v. A. B. Dick Company* U.S. Supreme Court decision in 1912 further solidified the manufacturer’s power over the patented product. This case upheld a mimeograph company’s (A. B. Dick) practice of requiring purchasers to use only those supplies (e.g., ink, stencils) obtained from A. B. Dick. Sporting goods manufacturers concluded that if the Court upheld the right of a licensee to use a patented product under certain circumstances, the Court might also uphold a similar system of contracts relating to RPM (“United States,” 1912).

## **■ THE CESSATION OF THE PATENT MONOPOLY**

### **The 1912 Oldfield Bill**

The 1912 Oldfield Bill, supported by Congressman Oldfield (Chairman of the Patent Committee of the House of Representatives), presented a great concern for the sporting goods industry. The Oldfield Bill specifically targeted the RPM tactics of manufacturers (Kops, 1912). The objective of the bill, according to Oldfield supporters, was to curtail the powers of the manufacturer of patented products. Advocates of the bill argued that the legalized RPM of patented products perpetu-

ated monopolies, inflated prices, and exploited the consumer. In contrast, the sporting goods industry argued that passage of the Oldfield Bill would be devastating for three reasons. First, as Charles Lent explained to readers of the *Sporting Goods Dealer*, the bill would bring about the demise of the jobber and wholesaler as products sold through discount houses and mail order catalogues would force traditional distributors to sell supplies near, or below, break-even figures ("Lent on Uniform Prices," 1912). This concern became paramount when the Parcels Post bill went into effect in 1913. The Parcels Post bill gave mail order houses a new advantage by lowering the cost of shipping packages that weighed under 11 pounds ("Parcel post," 1912). Second, the sporting goods industry argued that the bill would deceive the consumer as ruinous price cutting and loss leading practices would prosper. Third, the elimination of RPM would force the manufacturer to sell at lower margins and thwart existing or planned research and development (Dunlap, 1912). The sporting goods industry was pleased when this bill failed to be enacted.

### ***Bauer & Cie v. O'Donnell (1913)***

However, a year later the U.S. Supreme Court echoed the legislative sentiment in its 1913 decision in *Bauer & Cie v. O'Donnell*. The *Bauer* case involved the sale of Sanatogen, a water soluble protein, to a distributor who later sold the product to other vendees. The package contained the following language,

This size package of Sanatogen is licensed by us for sale and use at a price not less than one dollar (\$1.00). Any sale in violation of this condition . . . will constitute an infringement of our patent . . . . A purchase is an acceptance of this condition . . . (signed by) The Bauer Chemical Co.' (p. 8).

The Bauer Chemical Company sued a retail drug-store who sold the products for less than \$1.00. The Supreme Court distinguished between the facts of the *Henry v. A.B. Dick Co.* and decided in favor of the discounter. To the disappointment of the sporting goods manufacturers, the Supreme Court stated that the statutory right to vend a patented product ended once the manufacturer transferred the product title to another party. The sporting goods industry warned that the elimination of the patent holder's right to control the resale of patented goods would lead directly to a destruction of quality and lost jobs ("New re-sale," 1913).

## ■ **THE RIGHT TO UNILATERALLY REFUSE TO DEAL**

### ***U.S. v. Colgate & Co. (1919)***

The sporting goods industry welcomed the U.S. Supreme Court's decision in the 1919 case of *U. S. v. Colgate & Co.* ("Colgate Wins," 1919). The Colgate decision sanctified unilateral, independent actions between a manufacturer and the dealer "in the absence of any intent to create or maintain a monopoly" (*U.S. v. Colgate & Co.*, 1919, p. 307). Sporting goods manufacturers adopted this strategy of refusing to deal with price cutters before the turn of the century. For example, A.G. Spalding and Bros. instituted such a policy in 1899 in an attempt to increase business, stabilize market situations, and eliminate price cutting (Levine, 1985).



However, the *Colgate* decision gave sporting goods manufacturers the legal right to announce pricing policies (including the use of suggested or recommended prices or pre-ticketed items), and refuse to deal with distributors not adhering to the announced policy.

Although the *Colgate* decision gave the manufacturers the right to refuse to deal with discounters, resultant dealer terminations often ignited antitrust suits. The plaintiff discounter frequently alleged that the manufacturer's refusal to deal constituted a conspiracy between a manufacturer and other distributors to restrain trade by enforcing or coercing all distributors to maintain resale prices. These legal challenges reveal that the Supreme Court narrowly interprets the *Colgate* doctrine (*FTC v. Beech Nut*, 1922; *United States v. Bausch & Lomb*, 1944; *United States v. Parke, Davis & Co.*, 1960).

The sporting goods industry was victimized by this narrow interpretation into the 1970s. For example, in 1972 the FTC ruled that Browning Arms Co. conspired with its authorized dealers by:

- a. Regularly furnishing dealers with price lists,
- b. Requiring dealers in non-Fair Trade states to enter agreements to maintain sales prices,
- c. Requiring dealers to sell only to authorized dealers (i.e., non-discounters),
- d. Securing dealers "cooperation and assistance in identifying and reporting dealers who advertise, offer to sell or sell respondent's product's at prices lower than its established resale prices," and
- e. "Directing its salesmen, representatives, and other employees to secure and report information identifying any dealer who fails to adhere to and maintain its established resale prices" (p. 750).

The Federal Trade Commission issued a cease and desist order requiring the Browning Arms Co. to eliminate the above practices. Similar FTC rulings were issued against Ithaca Gun Company, Inc. (1971), Colt Industries Operating Corp. (1974), Medalist Industries (recreation tennis wear; 1976), Head Ski Co. (1968), United States Rubber Co. (Keds shoes; 1964, 1993), Jantzen Inc. (1964), and Cubco, Inc. (ski bindings and related ski equipment; 1975).

## ■ THE ERA OF FEDERAL AND STATE INTERVENTION

### **The National Industrial Recovery Act (1933)**

RPM continued to be a competitive concern to the sporting goods industry throughout the economic trauma which characterized the early 1930s. The National Industrial Recovery Act (NIRA) of 1933 was passed in an effort to stabilize the economy and bring about industrial successes. The various industries themselves, such as the sporting goods industry, played a paramount role in the NIRA's plan. Title 1, section 3 of the NIRA encouraged firms within various industries to cooperate among themselves in the defining and monitoring of fair trade practices. The defined fair trade codes, when signed by the President, had the power of the law. The sporting goods industry, strong advocates of RPM, lobbied behind Congressman Kelly who fought to include a section in the NIRA legalizing RPM in interstate

commerce. Congressman Kelly's inclusion, appearing in Section 4(a), reads,

The President is authorized to enter into agreements with, and to approve voluntary agreements between and among, persons engaged in a trade or industry, labor organizations, and trade or industrial organizations, associations or groups, relating to any trade or industry, if in his judgment such agreements will aid in effectuating the policy of this title with respect to transactions in or affecting interstate or foreign commerce . . . (p. 390).

The stated "voluntary agreements" above included RPM practices. This enabling language was viewed as a victory by RPM advocates. The sporting goods industry began devising its own industry fair trade codes as early as 1931. All of the proposed codes supported RPM as a fair trade practice.<sup>1</sup> However, when the proposed codes were presented to NIRA officials, the language supporting RPM practices was altered. J. R. Hawkinson, a member of the NIRA Code Authority, opposed RPM. "The setting of prices," he said, "is undesirable from the competitive point of view" (Meeks, 1934, p. 81). In the face of such opposition, the sporting goods code developers resorted to the *Colgate* doctrine of 1919 and the wording of the RPM sections became more abstract. For example, the language of the 1933 Athletics Goods Industry revised code (section 8) read as follows:

No member of the industry shall . . . fix a price. . . where the effect . . . may be to substantially lessen competition or tend to create a monopoly in any line of commerce . . . Nothing contained shall prevent persons engaged in selling the products of this industry in commerce from selecting their own customers in bona fide transactions and not in restraint of trade ("Revisions," 1933, p. 93)

The U.S. Supreme Court declared the NIRA unconstitutional in the *Schechter Corp. v. United States* decision (1935) because it exceeded the power of Congress to regulate interstate commerce and interfered with the constitutional power granted to the States.

### **Fair Trade Laws**

The Fair Trade laws had a major impact on RPM practices. The Fair Trade laws were state enactments which permitted manufacturers or distributors of brand name goods to legally contract with distributors to fix minimum resale prices. Manufacturers could only establish RPM in those states which had enacted Fair Trade laws. California enacted the first Fair Trade law in 1931. Between 1933 and 1937, fair trade laws were operative in 14 states. By 1941, 45 states had adopted Fair Trade laws. However, as recognized by California in the early 1930s, Fair Trade laws which legalized RPM agreements between a manufacturer and one distributor were ineffective as non-contracting parties (e.g., the discounters) continued to sell below cost. Distributors were soon unwilling to enter into a RPM contract with a manufacturer when competitive pressures resulted in ruinous price competition.

The nonsigner clauses evolved as a remedy to the above problem. The nonsigner provision stated that if a particular manufacturer made a RPM agreement with one distributor, then all distributors selling the manufacturer's products in that particular state were also bound by the RPM agreement. California was the first state to include a nonsigner provision in its Fair Trade law (1933). Similar nonsigner

provisions were quickly added as amendments to the Fair Trade laws of other states (Grether, 1936; Yamey, 1966).

The sporting goods industry favored Fair Trade laws as they gave manufacturers a legal outlet to enforce RPM. Leaders in the sporting goods industry realized the necessity of cooperation among manufacturers, distributors, and retailers from the earlier NIRA experience. The National Sporting Goods Association also encouraged the industry to voluntarily police Fair Trade laws as it recognized that enforcement by the law would be a slow and cumbersome process (Bradley, 1938). Sam Monetta, president of the Ohio Sporting Goods Association, was one of the first to organize the manufacturers, distributors, and retailers within his state to better enforce the Ohio Fair Trade Act. For example, Monetta requested that all manufacturers file RPM policies with the state. Further, RPM enforcement measures were to be explained to dealers at state and local meetings. Monetta's voluntary monitorship and enforcement ideas were copied by other state sporting goods associations in Illinois, Indiana, Kentucky, Michigan, West Virginia, New York, and Pennsylvania ("Sam Monetta," 1938).

## ■ THE DECADES OF JUDICIAL AND CONGRESSIONAL VACILLATION

### ***Old Dearborn Co. v. Seagram Corp. (1936)***

The *Old Dearborn Co. v. Seagram Corp.* case in 1936 is significant as it addressed the constitutionality of the nonsigner clause. The appellant in the *Old Dearborn* case sold the appellee's product at discount prices regardless of the Fair Trade laws and existing RPM agreements made with other distributors. The appellant, well aware of the existing RPM agreements, refused to adhere to the appellee's pricing structure and alleged that the nonsigner provision of the Illinois Fair Trade law interfered with an individual distributor's constitutional right to dispose of property. To the relief of the sporting goods industry, the U.S. Supreme Court in the *Old Dearborn* case upheld the constitutionality of the nonsigner clause for two reasons. First, the Supreme Court argued that individual distributors are not compelled to purchase a manufacturer's RPM products and cannot, therefore, be denied a property right. As explained by the Court, the appellants voluntarily acquired the property with full knowledge of the RPM restrictions. Consequently, the appellants should be expected to adhere to the law legalizing Fair Trade practices. Second, the Supreme Court recognized that there are actually two titles associated with every product. As explained by the Supreme Court in *Old Dearborn Co.* (1936), a commodity's value consists of the product itself in addition to the goodwill reflected by its trademark or brand name. As explained by the Court, "There is a great body of fact and opinion tending to show that price cutting by retail dealers is not only injurious to the good will and business of the producer and distributor of identified goods, but injurious to the general public as well" (p. 195).

The necessity of the nonsigner clause was very apparent to the sporting goods industry. The *Colgate* doctrine provided sporting goods manufacturers with the

legal right to announce in advance the circumstances under which they would deal with distributors. Further, it granted manufacturers the right to refuse to sell to distributors that violated the publicized policy. However, as noted earlier, the Supreme Court's application of the *Colgate* doctrine severely limited its impact upon RPM practices. Without the nonsigner clause, unified RPM was impossible and beyond the control of the sporting goods manufacturer.

### **The Miller-Tydings Act**

The constitutional challenges of the Fair Trade laws prompted the passage of a federal statute in 1937, the Miller-Tydings Act, to solidify the legality of the Fair Trade laws. The Miller-Tydings legislation legalized fair trade in all states for trademarked or branded products in free and open competition with similar products. RPM critics fought against the passage of this legislation and argued that RPM inflated consumer prices while providing the manufacturer and distributor with excessive profits. The advocates of this bill argued that the clause of the Miller-Tydings Act requiring that products be in "free and open competition" with similar products would prevent inflationary prices and consumer exploitation. For example, a company with a monopoly on total product output would be refrained from charging exorbitant prices at the expense of the consumer. In comparison, monopolistic companies competing for market share are not likely to price products outside the consumer's expected price threshold. For example, in 1937 there were 247 sporting goods manufacturing companies in competition with each other (Census of Manufacturers, 1937). It is unlikely that any one company would adopt a high-priced resale maintenance system because of the ease of product substitutability. As explained within the May, 1955 issue of the *Sporting Goods Dealer*, Fair Trade laws and their advocates were seeking a means to control ruinous competition brought about by the discount stores ("Pricing for Profit," 1955). There was no intent to exploit the consumer via high prices and exorbitant profit margins.

The passage of the Miller-Tydings Act was welcomed by sporting goods manufacturers as they had advocated the enactment of fair trade laws since the beginning of the twentieth century. For example, Maxwell, Iver Johnson's Arm & Cycle Company Sales Manager, predicted the need for a federal law legalizing intra-state RPM as early as 1911 ("The Supreme Court Speaks," 1911). The June, 1911 issue of the *Sporting Goods Dealer* quotes Maxwell as saying,

What is really needed is a Federal law which will give the manufacturer of unpatented articles the right to control their resale price so long as he does not act in concert with other manufacturers (p. 58).

### ***Schwegmann Brothers v. Calvert Corp. (1951)***

Nonsigner clauses were effective until the 1951 U.S. Supreme Court decision in *Schwegmann Brothers v. Calvert Corp.*. In this decision the Supreme Court invalidated the nonsigner clause for two reasons. First, the Court questioned the legality of forcing individuals to abide by a contract of which they were not a willing party. As explained by the Supreme Court, the nonsigner clause seeks,

To impose price fixing on persons who have not contracted or agreed to the scheme . . . That is not price fixing by contract or agreement; that is price fixing by compulsion. That is not following the path of consensual agreement; that is resort to coercion (p. 388).

Second, the Supreme Court looked to the intent of the legislation as inferred from the specific language of the Miller-Tydings Act. As noted by the Court, the Act itself contained no mention of the nonsigner clause. Rather, the Miller-Tydings act addressed only “contracts or agreements prescribing minimum prices for resale.” The Supreme Court argued that the absence of the nonsigner provision indicated that the framers of this federal law did not intended to impact a non-contracting party (i.e, the distributor).

### **The McGuire Act**

The unwelcome *Schwegmann Brothers* decision prompted the sporting goods industry to lobby for legislation which would once again validate the non-signer clause of state fair trade laws (“Fair Traders,” 1951). Although RPM was declared a violation of the Sherman Act in the *Dr. Miles* case, the Supreme Court left an available loophole for RPM advocates when it stated that a manufacturer cannot fix prices in the “absence of a contract or statutory right” (*Dr. Miles Medical Co. v. Park & Sons Co.*, 1911, p. 405). The McGuire Act, passed in 1952 as an amendment to the Federal Trade Commission Act, nullified the *Schwegmann Brothers* court decision and once again legalized the nonsigner clause of the state fair trade acts (15 USC 45). As stated, the purpose of the McGuire Act is,

To protect the rights of States under the United States Constitution to regulate their internal affairs and more particularly to enact statutes and laws, and to adopt policies, which authorize contracts and agreements prescribing minimum or stipulated prices for the resale of commodities and to extend the minimum or stipulated prices prescribed by such contracts and agreements to persons who are not parties thereto (p. 632).

The McGuire Act once again mandated that all intra-state distributors adhere to a manufacturer’s RPM policy when any one distributor in that particular state entered into a RPM agreement.

The fair trade laws, adopted by 45 of the 48 states, continued to dominate all aspects of the sporting goods industry during the 1950s. Conventions, board meetings and association meetings all focused on this issue. The sporting goods industry feared that the ruinous price competition existing prior to World War II would again emerge. The fair trade laws and their non-signer provisions were viewed by leaders in the sporting goods industry as a way to control extant price cutting (Autz, 1945). Articles in the *Sporting Goods Dealer* conveyed the problems of selling below fair trade to the retailer (Autz, 1945; Civitello, 1945; “Evils of Cutting Prices,” 1947). For example, a retailer who discounted a product by 5% would be forced to sell 25% more of a particular product (i.e., volume) to offset the discount (“Evils of Cutting Prices,” 1947). Retailers forced to compete on volume further magnified the retailer’s need to engage in deceptive trade practices. Further, the National Sporting Goods Association and the Associated Fishing Tackle

Manufacturers argued that in addition to price wars, relaxed credit, inflation, and slow moving inventories presented problems for the sporting goods industry ("Fair Trade Advocates," 1952).

A survey performed by the *Sporting Goods Dealer* estimated that 40% of all sporting goods were fair traded in 1951. Most of these goods were fishing tackle and arms and ammunition products. Articles appearing in the *Sporting Goods Dealer* encouraged additional manufacturers of athletic equipment to join the fair trade allegiance ("Fair Traders," 1951). A 1955 survey conducted by the *Sporting Goods Dealer* revealed that the majority of those involved in the sporting goods industry favored Fair Trade laws. For example, the survey indicated that 45.1% of the manufacturers, 73.4% of the jobbers, and 71.9% of the retailers favored fair trade laws.<sup>2</sup>

The McGuire Act comforted RPM advocates who feared the decision of the earlier *Schwegmann* decision. However, sporting goods manufacturers remained sensitive to possible constitutional challenges of the state laws. For example, Shakespeare Company, a manufacturer of fishing tackle and related equipment, sued Lippman's Tool Shop Sporting Good Company in 1952 alleging infringement of the Michigan Fair Trade laws (*Shakespeare Co. v. Lippman*, 1952). The Supreme Court of Michigan held that Michigan's Fair Trade Act was unconstitutional as it violated a nonsigner's due process clause.<sup>3</sup>

Remington also brought suit in 1954 against a discount house allegedly selling rifles and ammunition below Remington fair trade prices. Remington later withdrew the lawsuit as it feared the Colorado Supreme Court would similarly test the constitutionality of the Colorado Fair Trade act ("Remington," 1954). As of July, 1955, a number of state courts (e.g., Arkansas, Florida, Georgia, Michigan, and Nebraska) had held that the nonsigner clauses within state Fair Trade laws were unconstitutional (Conference Board, 1955). By 1960, 16 states had declared their fair trade laws unconstitutional.

Sales-below-cost statutes prospered during this era of constitutionality inquiry. Thirty-one states had enacted sales-below-cost statutes by 1956. The statutes prohibited "sales, offers of sales, or advertisements of sales below the sellers's cost" (Jones, 1960, p. 905). Violators were subject to both civil and criminal penalties. These statutes provided security to manufacturers distributing products in states whose Fair Trade laws were declared unconstitutional. Further, the sales-below-cost statutes protected manufacturers against the discounting measures of mail-order houses located in non-fair trade jurisdictions (Jones, 1960).

The constitutional challenges of the fair trade laws, the Supreme Court's strict interpretation of the Colgate doctrine, and the lack of uniformity among the state's selling-below-cost statutes ignited the immediate need for a federal solution to industry's pricing woes. Numerous bills were proposed which would have legalized RPM practices at the federal level. For example, Senate bill 1722, the Maddin bill, the Steed bill, the anti-loss leader bill, and the Harris bill all empowered manufacturers to establish legalized RPM practices (Sandifer, 1959; Sandifer, 1960a; Sandifer, 1960b; Sandifer, 1961). RPM and fair trade advocates lobbied behind the passage of these bills as they would have eliminated discounting practices and the constitutional uncertainties of fair trade. Further, the proposed bills, in comparison

to the Supreme Court's subsequent interpretation of the *Colgate* decision in 1919, provided the manufacturer with the right to actively investigate and monitor distributors' resale prices. Unfortunately for RPM advocates, none of these bills was ever enacted.

### **The Consumer Goods Pricing Act of 1975**

The sporting goods industry ardently supported RPM beginning in the late 1800s. In each of the stages covered in this brief history, the sporting goods industry argued that RPM was necessary as it protected the manufacturer, distributor, and consumer against unscrupulous sellers. Manufacturers, distributors, and consumers all began to question the validity of such arguments during the 1970s.

In 1975, the Consumer Goods Pricing Act repealed the Miller-Tydings Act of 1937. As explained in a 1975 Senate Report, the repeal of the Fair Trade laws was supported by,

President Ford, consumer groups, the Justice Department, the FTC, the Council on Wage and Price Stability, discount stores and smaller business associations. Editorials in newspapers across the country unanimously favored the repeal (p. 127).

Opponents viewed Fair Trade laws as obsolete and inefficient. These opponents scorned the connotation "fairness" exuded by the Act's title. The inflationary era of the 1970s further escalated consumer unrest. Price sensitive consumers were no longer convinced that RPM was being used to stimulate competition and economic activity while benefiting the consumer. Their arguments attacked RPM practices for four reasons.

## **■ ARGUMENTS AGAINST RPM**

### **Encourages inflationary prices**

Consumers believed that manufacturers and distributors were abusing RPM and reaping excessive margins at the consumers' expense. As noted in the research (Senate Report, 1975; Weisel, 1988), prices were between 18-27% higher in states with fair trade laws. For example, a bicycle listing for \$300 in a fair trade state could be purchased in a non-fair trade state for just over \$200. A similar study estimated that consumers would be saved \$1.2 billion per year with the abolition of fair trade statutes. Further, Canada and Great Britain repealed their Fair Trade laws in 1957 and 1965, respectively, and there was no evidence documenting the ruinous consequences associated with price competition.<sup>4</sup>

### **Facilitates cartel establishment**

Opponents of RPM argue that RPM supports both manufacturer and retailer cartels while placing the consumer and other small business competitors at a disadvantage (Arquit, 1992; Weisel, 1988; Yamey, 1966). As argued by RPM critics, manufacturer cartels allowed the manufacturers within an industry to use RPM as a means to fix prices horizontally. Manufacturers, knowing the RPM policies of their competitors, priced similar products at similar prices. This horizon-

tal pricing scheme absolved manufacturers from the burdensome task competing on a cost basis while allowing them to reap above average profit margins. Individuals considering entrance into an industry faced the retaliation efforts by the group of horizontal conspirers as they had the necessary monies needed to discourage the new entrant's success through elaborate marketing campaigns, product innovation, or service offerings. A retailer cartel benefits from RPM as new entrants are discouraged to enter an established market when unable to realize the market share benefits associated with low cost distribution (Yamey, 1966). Evidence supporting the established entry barriers created by RPM was reported in Senate Report No. 94-466. As noted in the report, the number of retail entrants in non-Fair Trade states increased 32% more than the number of retail entrants in states with Fair Trade laws. Further, the report indicated that states with Fair Trade laws have a 55% higher rate of business failures than non-Fair Trade states. As summarized by Weisel (1988, p. 1442), "Dealer and manufacturer cartels represent horizontal collusion clothed in vertical form."

### **Fair trade proved too expensive for the small manufacturer**

Small sporting goods manufacturers, the proposed recipients of Fair Trade laws, came to view Fair Trade as an "expensive luxury." Sporting goods companies realized that the enforcement of Fair Trade laws required significant monies and a great deal of time. For example, in 1957 the Enterprise Manufacturing Company (fishing tackle manufacturers) spent in excess of \$10,000 to prosecute one violator (Autz, 1957a). The Enterprise Manufacturing Company was one of the few sporting goods companies that could afford to spend \$10,000 to prosecute one violator as it was a large, well established company. However, most sporting goods companies were not in the same financial position as the Enterprise Manufacturing Company. Further, as explained by Enterprise's company President, J.S. Pflueger, convicting one of violating Fair Trade laws was ineffective. For example, as Enterprise was challenging the one violator at an expense of \$10,000, two other violators emerged and would have to be independently prosecuted also (Autz, 1957a).

Herman's study and the reports from select governmental committees agree that it is the large manufacturer, not the small manufacturer, engaging in fair trade practices (Herman, 1959; Senate Report, 1956). The products of the small manufacturer, without the monies to compete with the established brand products, do not need price maintenance for two reasons. First, it is unlikely that distributors will use the products of a small manufacturer as loss leaders. Consequently, the small manufacturer is not impacted by the evils associated with loss leading selling. Second, it is more likely that the small manufacturer will favor a penetration pricing policy, versus RPM, in an effort to compete on price and increase generated sales.

## **■ THE DORMANT PERIOD**

The Consumer Goods Pricing Act signaled, once again, the *per se* standard of RPM illegality under the Sherman Act as decided 64 years earlier in the *Dr. Miles* case. However, the views of federal agencies (e.g., FTC, Department of Justice) and



the legislature varied dramatically (Denger, 1992). Pro-competitive effects of RPM were supported for a few years by the Federal Trade Commission Chairman, J. C. Miller, III and the Assistant Attorney General in charge of antitrust, W. F. Baxter (Gatty, 1982; Kornblum, 1983). Both Miller and Baxter felt the *per se* illegality of RPM reflected bad economic judgement. For example, RPM protects new competitors against product price cutting and image devastation and encourages distributors to provide the necessary service provisions. Baxter also provided editorials to sporting goods publications encouraging manufacturers to engage in RPM (Fitzgerald, 1983). Mike Fitzgerald, Marketing Vice-President of Sportmart, Inc., estimated in 1983 that 95-100% of all manufacturers would adopt RPM practices if they were declared a legal practice (Fitzgerald, 1983). Consequently, neither of these individuals pursued RPM allegations against manufacturers, regardless of a number of complaints, for over a 15-year period (Kornblum, 1983; "Study's findings," 1984). However, disgruntled plaintiffs could still file private suits alleging a manufacturer's RPM practices violated the antitrust laws.

With Miller's prodding, the FTC also considered exempting manufacturers with market share below 8-10% from RPM illegalities for two reasons. First, Miller argued that a new manufacturer cannot afford to have its investment in advertising and capital bastardized by price cutters. Second, Miller argued that RPM provides the incentive for distributors to partake in extensive service offerings. Miller recognized these service provisions of the distributor as critical when introducing a new product. Miller and Baxter also advocated the rule of reason analysis versus *per se* judgements regarding RPM (Gatty, 1982; Kornblum, 1983). On the other hand, senators, opposed to both Miller and Baxter, launched an extensive inquiry into the FTC operations, encouraged delayed funding for the Justice Department until it stopped supporting RPM in the courts, and even called for Baxter's resignation (Kornblum, 1983).

## ■ THE SUPREME COURT'S INDIRECT SUPPORT FOR RPM

### ***Continental T. V., Inc. v. GTE Sylvania Inc. (1977)***

The *Continental T. V., Inc. v. GTE Sylvania Inc.* in 1977 was significant as the U.S. Supreme Court overruled prior decisions<sup>5</sup> and held that non-price vertical restraints (e.g., territorial restrictions) were not illegal *per se* and should be examined under the rule of reason standard. Although this case did not directly address RPM and its post-Fair Trade *per se* illegality, RPM advocates suggested that this case would serve as precedent for subsequent decisions applying the rule of reason standard to vertical price restraints as well.<sup>6</sup>

### ***Monsanto v. Spray-Rite Service Corporation (1984)***

Similar to the *Continental* decision, the U.S. Supreme Court's decision in *Monsanto v. Spray-Rite Service Corp.* (1984) did not directly address the *per se* illegality of vertical price restraints (e.g., RPM), but it did prove to be a victory for RPM advocates. This case strengthened the ability of a manufacturer to refuse to

deal by requiring the plaintiff to produce a much greater degree of proof when alleging that an injury occurred as a result of a manufacturer's coercive activity. Monsanto terminated Spray-Rite because it was not providing adequate customer services. Spray-Rite sued and alleged that the termination was the result of a conspiracy among the manufacturer and its dealers in violation of the antitrust laws. Specifically, Spray-Rite alleged that it was terminated as a result of complaints from competing distributors who were unhappy with Spray-Rite's policy of selling below Monsanto's suggested resale prices. The Court held that the termination based upon competing dealer complaints was not sufficient evidence to indicate a RPM conspiracy. As explained by Justice Powell,

There must be evidence that tends to exclude the possibility of independent action by the manufacturer and distributor. That is, there must be direct or circumstantial evidence that reasonably tends to prove that the manufacturer and others had a conscious commitment to a common scheme designed to achieve an unlawful objective (p. 768).

The impact of the Monsanto decision is two-fold. First, it forces disgruntled distributors to engage in a time-consuming, expensive task to uncover "direct and circumstantial" evidence implicating a manufacturer allegedly involved in a "conspiracy to restrain trade." In fact, literature suggests that many claims will not survive summary judgment as a result of the perceived inability to gather the necessary "direct and circumstantial evidence" (Aalberts, 1989; Aalberts and Day, 1989). Second, Aalberts and Day (1989) argue that this decision will force discounters and chain stores to either comply with a manufacturer's RPM policy or risk having supplies terminated.

The sporting goods industry welcomed this decision as sporting goods manufacturers have always been besieged with disgruntled wholesalers, jobbers, and retailers when these distributors are forced to compete with the discounter (Autz, 1957a). The *Monsanto* decision provides manufacturers greater freedom from liability when choosing whether to terminate discount dealers or uncooperative wholesalers or distributors.

### ***Business Electronics Corp. v. Sharp Electronics Corp. (1988)***

The 1988 U.S. Supreme Court decision in *Business Electronics Corp. v. Sharp Electronics Corp.* again favored RPM advocates. This case involved the allegation that Sharp Electronics, a retailer of Business Electronic's products, was terminated after Harwell, a competing retailer, complained about the price-cutting policies of Business Electronics. Harwell told Sharp Electronics to either cease doing business with Business Electronics or Harwell would refuse to carry Sharp's products. Sharp subsequently terminated its relationship with Business Electronics. Business Electronics sued alleging that its termination resulted from a pricing conspiracy between Harwell and Sharp Electronics in violation of § 1 of the Sherman Act. The Court ruled in favor of Business Electronics for two reasons. First, Sharp Electronics was unable to prove that the alleged conspiracy was anti-competitive or economically unreasonable. Second, the Court explained that a conspiracy to restrain trade cannot be inferred from the independent actions of a manufacturer. In the wake of the

*Business Electronics* decision, courts have refused to apply the *per se* analysis without evidence of an RPM agreement.<sup>7</sup>

## ■ LEGAL WAYS TO MAINTAIN RESALE PRICES

As this brief history has pointed out, the legality of RPM has been, and continues to be, in a state of flux. However, at the present time, manufacturers intent on maintaining resale prices have five legal options.

### **Unilateral refusal to deal**

The 1919 *Colgate* doctrine, although narrowly construed, still allows manufacturers to announce their pricing policy and then refuse to do business with distributors who fail to adhere to the suggested or recommended practices. For example, Nike only recently conceded to competitive pressures and began distributing its product through The Sports Authority, a mass discount distributor.

However, manufacturer's who coerce compliance with a pricing policy are often implicated for organizing an unlawful price maintenance combination (Benton and Gross, 1993). Coercion is typically a question of fact. However, there is established precedent which questions a manufacturer's intentions when, for example, price-cutting distributors are terminated, become the recipients of defective goods, or receive only partial orders (Benton and Gross, 1993). In addition, withholding dealer assistance,<sup>8</sup> refusals to deal without legal cause, policing the pricing tactics of distributors, sending memorandums delineating specific pricing policies,<sup>9</sup> and using short-term consignment agreements that are not renewed unless product is sold at a specific price<sup>10</sup> are all indicative of a collective "combination" or "conspiracy" to eliminate distributors who fail to adhere to RPM practices.

### **Licensing a patented product**

It is illegal for the patentee of a patented article to control the price of a distributor once title has passed to the buyer/distributor. However, a manufacturer is allowed to fix the price of a product when product distribution occurs through a genuine licensee in competition with the manufacturer. The U.S. Supreme Court confirmed the right of a patentee to fix the price of products distributed to a genuine licensee in the 1926 case, *United States v. Gen. Elec. Co.*. As explained by the court, a patentee is granted a patent monopoly as an inducement to innovate and enhance economic and societal welfare. The opportunity to acquire a profit is part of the granted monopoly. A licensee distributing products at a discount would likely usurp the market share of the inventor. This type of action would be antithetical to patent law and consequently, does not constitute illegal RPM in violation of the Sherman Act. A patentee, however, would not be able to control the resale price of a product once the product is re-sold by the licensee.

However, court decisions caution manufacturers who establish license agreements distribution in two situations. First, manufacturers with a large portion of the industry's market share, using multiple licensees, and stipulating resale prices may represent an industry-wide conspiracy to fix prices. As stated in the 1948 case,

*United States v. Gypsum Co.*, such action goes beyond any protection provided by the patent laws.<sup>11</sup> Second, the Supreme Court decided in *United States v. Line Material Co.* (1948) that cross-license agreements also go beyond any protection provided by the patent laws. As explained by the Court, an illegal cross-license agreement would occur when,

Two or more patentees with competitive, non-infringing patents combine them and fix prices on all devices produced under any of the patents (p. 311).

As noted by the Court, cross-licensing for RPM purposes impedes competition in violation of the antitrust laws.

### **Consignment**

Consignment selling is a legal option for manufacturers intent on retaining an established resale price. In a consignment relationship, the manufacturer sends inventory to the distributor without surrendering product title and control. The major obstacle associated with the establishment of a consignment system focuses on the authenticity and legality of the system itself. Manufacturers establishing consignment systems, in name only, for the sole purpose of RPM will not be cloaked with antitrust immunity (*Simpson v. Union Oil Co*, 1964). Determinative questions regarding the authenticity of a consignment system focus on the amount of business risk retained by the manufacturer. For example, a manufacturer engaged in a legal consignment agreement would: a) retain title to the goods, b) pay the taxes (e.g., property, inventory, sales) on the goods, c) bear the risk of unsold goods, defective goods, and bad-credit sales, d) and, of course, establish the resale price.

### **Vertical integration**

Vertical integration allows the manufacturer to legally establish resale prices by selling directly to the ultimate consumer through either owned wholesale and retail outlets, a company sales force, and/or mail-order systems. However, vertical integration is not an absolute price control remedy for sporting goods manufacturers for two reasons. First, it is an expensive alternative. Second, the integrated company could not establish resale prices for goods sold through non-owned retail outlets as this would represent horizontal price fixing, a *per se* illegality in violation of the antitrust laws. As explained by Yamey (1966),

Since both the Miller-Tydings and McGuire Acts contain specific statements that their provisions do not legalize agreements **among** manufacturers, **among** wholesalers, or **among** retailers, federal and state courts and administrative agencies have ruled that vertically integrated firms may not establish resale prices for their competitor-customers (p. 71-72).

Vertical integration by acquisition escalated in 1993. Six sporting goods companies were involved in acquisitions at a total estimated price of \$750 million (Ryan, 1994).

### **Conclusion**

The legality of RPM practices has vascillated throughout the years. Statutes and Supreme Court decisions offered RPM proponents the most stability during the

early era of the patent protection and the later decades of the fair trade laws. The dormancy, or inaction, experienced during the late 1970s and throughout the 1980s has left the legality of RPM practices in a somewhat dubious state. However, the future of legalized RPM practices depends upon who is on the U.S. Supreme Court and who is residing in the various administrative offices (Vandeventer, 1994). For example, the Supreme Court has not recently addressed whether RPM, a vertical price restraint, should be analyzed under the *per se* or rule of reason analysis. The outcome of this decision will be influenced by the individuals on the Supreme Court and how they interpret restraints of trade as prohibited by the Sherman Act. In addition, the Supreme Court's interpretation and application of the *Colgate* doctrine will continue to impact the manner in which a manufacturer chooses to maintain resale prices. Further, as noted by Denger (1992), the FTC Chair, the Attorney General at the federal level, and the state Attorney's General also influence how aggressively RPM cases are pursued.

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<sup>0</sup> A per se violation precludes the defendant from introducing any evidence which may prove pro-competitive effects as the restraint itself (e.g., RPM) is automatically viewed as being “inherently pernicious, lacking any redeeming virtue” (*Northern Pa. R. Co.*, 1958).

<sup>1</sup> For example, the Fishing Tackle Manufacturing Code, the Sporting Goods Distributors Code, the Athletics Goods Industry Code, the Small Arms and Ammo Code, the Billiards and Bowling Code, and the Bicycle Code. See the *Sporting Goods Dealer*, 1933.

<sup>2</sup> The majority of manufacturers were in favor of fair trade. However, the expense and time associated with the enforcement of the fair trade laws was overwhelming for most small sporting goods manufacturers. This factor explains, in part, the seemingly low survey response of 45.1%.

<sup>3</sup> The court argued that the Fair Trade Act was not within the purview of the police power of the state. Police power allows states to adopt legislation related to public morals, health, safety, or the general welfare of the public.

<sup>4</sup> However, the research findings regarding Fair Trade v. non-Fair Trade pricing practices are not absolute. For example, in comparison to the DOJ studies, Bowman (1955) found that during inflationary eras prices on non-fair traded items increased more than the prices of fair-traded items. Further, it is argued that these studies are deceiving for two additional reasons. First, the studies compare the prices of products which are sold as loss leaders in non-Fair Trade states (The Conference Board, 1955). The surveys fail to account for the volume of high-margin merchandise sold in selected non-Fair Trade stores (The Conference Board, 1955). Second, the studies fail to reflect differences in state-by-state cost-of-living standards.

<sup>5</sup> See *U. S. v. Bausch & Lomb Co.*, 321 U. S. 707 (1944) and *U. S. v. Arnold, Schwinn & Co.*, 388 U. S. 365 (1967).

<sup>6</sup> *The Standard Oil Co. v. U. S.* (1911) introduced the “rule of reason” analysis used when determining the legality or illegality of an alleged antitrust violation. The rule of reason requires the fact finder to review all allegations on a case-by-case basis with specific consideration given to the industry itself, conditions before and after the restraint is applied, the probable impact of the restraint, and reasons for adopting a particular restraint. Restraints which have pro-competitive effects are viewed as legal. For example, some restraints may be purely regulatory in nature and while they may hinder intrastate commerce they in effect benefit interstate commerce. For example, RPM restrains intrastate competition because it requires competing sellers to sell identical goods at the same prices. However, interstate competition is

enhanced as small retailers survive the dilemmas caused by price cutters and are protected against retaliatory measures of larger retailers. On the other hand, the per se analysis precludes the use of any defense or inquiry into the pro-competitive effects of the act itself (e.g., RPM). Rather, the act is perceived as “inherently pernicious, lacking any redeeming virtue” (*Northern Pa. R. Co.*, 1958).

<sup>7</sup> See *Toys “R” Us, Inc. v. R.H. Macy & Co.*, 728 F. Supp. 230 (S.D.N.Y., 1990); *Jeanery, Inc. v. James Jeans, Inc.*, 849 F.2d 1148 (9th Cir. 1988).

<sup>8</sup> See *Lehrman v. Gulf Oil Corporation*, 464 F.2d 26 (5th Cir.), cert. denied sub nom. *Gulf Oil Corp. v. Lehrman*, 409 U.S. 1077 (1972).

<sup>9</sup> See *Phillips v. Crown Central Pet. Corp.*, 602 F.2d 616 (4th Cir. 1979) cert. denied 444 U.S. 1074 (1980).

<sup>10</sup> See *Simpson v. Union Oil Co.*, 377 U.S. 13, rehearing denied 377 U.S. 949 (1964).

<sup>11</sup> See also *United States v. Sealy, Inc.*, 388 U.S. 350 (1967) and *Superior Bedding Co. Serta Assoc., Inc.*, 353 F. Supp. 1147 (1972).