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Minimum Resale Price Maintenance Agreements: Economic & Commercial Justifications

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Just as antitrust economists cannot operate in a legal vacuum, the modern competition lawyer, in practice or academia, has to have a strong knowledge of antitrust economics.[1]

ABSTRACT: *Minimum Resale Price Maintenance agreements are considered anti-competitive in most jurisdictions – both developed and developing – because of their perceived ability to distort price competition between retailers. Economic objective of infusing competition at all levels is to ensure efficiency that leads to consumer welfare in the form of reduced prices and a wider range of choices. The paper begins with challenging the basic assumption that 'reduced prices always lead to consumer welfare'. The primary proposition set out in the paper is that intra-brand price competition between retailers neither conclusively indicates efficiency nor is welfare enhancing. Rather it adversely affects the intra-brand non-price competition and inter-brand competition in most situations. The paper also highlights how international organizations (UNCTAD, OECD, ICN and WTO), working towards bringing cooperation and convergence on different competition law issues, can work proactively in shaping the treatment accorded to minimum resale price maintenance agreements.*

1. INTRODUCTION

Competition law and economics are inextricable considering the usage of the latter in the former's evolution, formulation and interpretation. It is an accepted phenomenon that the application of economics in competition law not only provides predictability and precision in its execution, but also provides room for justifiable exceptions based on the efficiency proposition. The primary economic rationale behind competition law is efficiency creation that

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[1] Dr Mark Williams (NERA Director), 'The Role of Economics in Competition Law', *at* the Oxford University's BCL Competition Law course, 21 Oct. 2003.

results in price reduction, and thereby, allegedly, enhances consumer welfare.[2] Although the economic objectives of competition law include 'allocative efficiency', 'productive efficiency' and 'dynamic efficiency',[3] there is often a general misconception regarding the role of 'price' in ensuring consumer welfare which is why 'productive efficiency' is, at times, considered the sole or most important objective that competition law seeks to achieve.[4] And since it has been a perceived notion that there is a negative correlation[5] between product's price and consumer welfare, it is no wonder that competition authorities around the world strive to regulate and punish anti-competitive behaviour that can result in distortion of price competition. But a logical question that one is confronted with in such a situation is that – Is 'competitive price' (price reduction) the only agenda that competition law seeks (or should seek) to achieve? Is it only a low price that leads to consumer welfare? What if the non-price factors, that might push the price a little above the competitive price but, result in higher consumer welfare?

This sets out a fertile ground to study the treatment to which vertical price restraints, especially minimum Resale Price Maintenance ('RPM') agreements, are subjected to in different parts of the world. The dilemma of policy makers of whether to penalize or legalize minimum RPM agreements is evident not only from the difference in approaches employed by different countries but also by inconsistent approaches followed by some countries[6] over time.

It is an established position, both in law and economics, that RPMs destroy 'intra-brand price competition'.[7] This paper basically proclaims that 'intra-brand price competition' at the distributor's level is neither required nor is welfare enhancing. Rather, the imposition of minimum RPM agreement actually fosters the real competition among retailers/dealers[8] by shifting their focus from illusory price competition to the competition based on 'services' (pre/post sale).

Competition, no doubt, ensures that a firm has an incentive to find newer and better ways of reducing cost; otherwise, someone else will reduce their cost of production and take the market away from them.[9] But free competition at every stage and between stages vertically may not lead to consumer welfare. There is an apparent distinction between 'free'

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[2] Dr Mike Walker, Competition Law, Anti-Competitive Behavior and Merger Analysis: Economic Foundations, Asian Development Bank, available at http://www.adb.org/Documents/Others/OGC-Toolkits/Competition-Law/documents/competition_law_economic_foundations.pdf.

[3] Richard Whish (2009) *Competition Law* (New York: Oxford University Press, 6th ed.), 4. Allocative efficiency means the resources are so optimally allocated in the economy that it is not possible to make any one better off without making the other worse off. Productive efficiency means Productive efficiency is concerned with producing goods and services with the optimal combination of inputs to produce maximum output for the minimum cost. Dynamic efficiency means the producers will have the continuous desire to innovate for surviving and sustaining the consumer demand.

[4] Amit Bubna and Shubhashis Gangopadhyay (2007) 'The Economics of Competition Law', in *Competition Law Today – Concepts, Issues and the Law in Practice* (Vinod Dhall, ed., New Delhi: Oxford University Press), 444.

[5] Negative correlation between product's price and consumer welfare means an increase in price decreases consumer welfare and vice versa.

[6] US is a good example in this context where RPM was *per se* anticompetitive for as many as 96 years before it was held to be worthy of evaluation under the *rule of reason* approach.

[7] Ashley Doty (2008) 'Leegin v. PSKS: New Standard, New Challenges', 23 *Berkeley Technology Law Journal*, available at http://btlj.org/data/articles/23_1/655-684.pdf.

[8] Retailers and Dealers will be used interchangeably in this article and for the sake of simplicity intended to mean the same.

[9] Amit Bubna and Shubhashis Gangopadhyay (2007) 'The Economics of Competition Law', in *Competition Law Today – Concepts, Issues and the Law in Practice* (Vinod Dhall, ed., New Delhi: Oxford University Press), 444.

and 'fair' competition, while the former can lead to price minimization, the latter will lead to consumer welfare, in long run at least. This however, is not the subject or contention of this paper, and therefore not discussed here in detail. As per the argument set out in this paper, 'competition' which is fair and workable is the most effective. Therefore, if the non-price factors, that might push the price a little above the competitive price but, results in higher consumer welfare, there should not be any hesitation in legitimizing them.

The argument set forth in the paper, i.e. minimum RPM is welfare enhancing, initiates by focusing on the problems such as *'free riding'* and *'illusory intra-brand price competition'* that emerge as a consequence of outlawing RPMs by competition regulators. The existence of these problems as the most natural outcomes of a 'No-RPM'[10] world is corroborated by using the Game Theory analysis. The argument grows by putting forth the importance of useful pre-sale services which not only benefits the manufacturer in building and maintaining the demand for his product but also guides the consumer in making a well informed choice, at least in the case of 'experience goods'. The argument is demonstrated by employing an illustration of an 'experience good' (Perfume) and testing its probable behavior pattern in both, an RPM and a no-RPM hypothetical market framework.[11]

2. RESALE PRICE MAINTENANCE AGREEMENTS: AN OVERVIEW

A resale price maintenance (RPM)[12] agreement is a contract in which a manufacturer and a downstream distributor agree to a minimum or maximum price that the retailer will charge its customers.[13] This is often termed as a vertical price restraint as the manufacturer and downstream distributor are not operating at the same level of production cycle. Many jurisdictions treat such vertical price restraint as anti-competitive. In the U.S., presently, such agreements are evaluated and adjudged under the *rule of reason* approach.[14]

For decades, however, the position in the U.S. was not the same as it stands today. The venerable *Dr. Miles Medical* case[15] condemned *per se*[16] the resale price maintenance (RPM) agreements and such agreements were considered per se violative of antitrust law since 1911.

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[10] 'No RPM' world refers to situations and countries where RPM is considered to be anti-competitive and, therefore, is banned under the competition law.

[11] Although the author is conscious of the fact that the real-world application of competition law (including minimum RPMs) varies greatly between developed and emerging economy, the paper is kept more at a theoretical level without going into the cross-country application of minimum RPMs in detail.

[12] For the purpose of this article RPM, wherever not mentioned specifically, will mean minimum retail price mechanism.

[13] Kenneth G.Elzinga and David E. Mills (2008) 'The Economics of Resale Price Maintenance', in I*ssues In Competition Law And Policy* (Kenneth G. Elzinga & David E. Mills, eds.), ABA Section of Antitrust Law, 2008, *available at* SSRN: http://ssrn.com/abstract=926072.

[14] Michael A. Lindsay (2007) 'Resale Price Maintenance and the World After Leegin', 22(1) *Antitrust*.

[15] *Dr. Miles Medical Co. v. John D. Park*, 220 U.S. 373 (1911).

[16] *'Per se'* and *'rule of reason'* as approaches to evaluate the anti-competitive agreements were evolved by the US Supreme Court while interpreting different provisions of the US Antitrust Act (The Sherman Antitrust Act, 1890). A 'per se' violation requires no further inquiry into the practice's actual effects on the market or the intentions of those individuals who are engaged in the practice. Once the conduct falling under per se rule is established, the conduct is illegal without any inquiry into its actual competitive or anti-competitive effects. Juxtaposed to this is 'rule of reason' approach. Under this approach, along with the requirement of proving the existence of the alleged conduct (agreement), the complainant is also required to prove that such conduct's anti-competitive effects are more than it's pro-competitive effects.

It was only after Leegin's[17] when the US Supreme Court reversed Dr. Miles dicta and held that RPM is no longer condemned per se but is instead to be treated under the rule of reason.[18] So today RPM is no more a hard core restriction under the US Antitrust Law and is subject to 'rule of reason' approach, meaning thereby that the alleged agreement can be allowed if the pro-competitive benefits arising from such an agreement outdo the anti-competitive effects. Section 3(4) of the Indian Competition Act, 2002, enlists 'Resale Price Maintenance' agreement as a vertical anti-competitive agreement, though not subject to the 'shall presume' rule.[19] The approach, though not exactly equivalent, have some similarities to the 'rule of reason' approach used in the US.[20] In EU, the competition law, however, categorically presumes minimum resale price as a hard core restriction, though it adopts a lenient approach while dealing with the maximum resale price agreements. An agreement imposing maximum resale price can be exempted from the applicability of Art 101(1)[21] if the market share cap of 30% is not exceeded.[22] The minimum RPMs, on the other hand, have been condemned on various occasions. Even the 'New EU Vertical Restraint Regulations'[23] make it clear that resale price maintenance is a hardcore restriction and the exemptions and safe harbour provisions introduced in other vertical restraint agreements will not apply to vertical agreements that establish a fixed or minimum resale price. However, the new regulations recognize certain situations where RPM agreements could generate efficiencies.[24] Canada and Australia,[25] however, impose a 'per se' prohibition on resale price maintenance agreements.

A quick look on the legal provisions relating to RPM in various jurisdictions makes it clear that the confusion persists to cloud the legitimacy and acceptability of RPM as an efficiency enhancing tool. A dichotomy has existed primarily on *'per se'* versus 'rule of reason' approach, thereby ruling out the ability of RPM as 'generally efficiency enhancing'. Singapore, commendably, differs in its approach while dealing with the vertical agreements. Although Singapore's Competition Act is primarily on the lines of UK competition law, the

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[17] *Leegin Creative Leather Products, Inc., v. PSKS, Inc.*, 127 S.Ct. 2705 (2007).

[18] Kenneth G. Elzinga and David E. Mills (2010) 'Leegin and Procompetitive Resale Price Maintenance', 55 (2) *The Antitrust Bulletin* 349.

[19] The horizontal agreements like cartels, horizontal price arrangements, bid rigging etc. are presumed to be anti-competitive as per Sec 3(3) of the Indian Competition Act, 2002. For more detailed understanding of the approaches followed under the Indian competition law for evaluating horizontal and vertical anti-competitive agreements refer to 'Bhawna Gulati, Competition Law in India: Some Lacunas, Some Myths, Chartered Secretary, May 2012 (forthcoming)'.

[20] Vinod Dhall (2007) 'The Indian Competition Act, 2002', in *Competition Law Today – Concepts, Issues and the Law in Practice*, 509-11 (Vinod Dhall, ed., New Delhi: Oxford University Press).

[21] Formerly Article 81(1) of the EC Treaty.

[22] Richard Whish (2009) *Competition Law* (New York: Oxford University Press, 6th ed.).

[23] Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices (OJ 2010 L 102, p. 1), replacing Commission Regulation (EC) No 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices (OJ 1999, L 336, p. 21). The New Guidelines can be found at: http://ec.europa.eu/competition/antitrust/legislation/guidelines_vertical_en.pdf.

[24] Howard T. Rosenblatt, Eric Barbier de La Serre & Gianni De Stefano (2010) *The New EU Vertical Restraints Regulation: Navigating the Vast Seas Beyond Safe Harbors and Hardcore Restrictions*, Client Alert (Latham & Watkins Litigation Department), 26 April 2010, available at http://www.lw.com/upload/pubContent/_pdf/pub3502_1.pdf.

[25] In Australia, RPM agreements are per se illegal for both goods and services but can be authorized on public benefit grounds.

provisions relating to vertical restraints are different. Third Schedule very specifically states that, Section 34[26] prohibition shall not apply to any vertical agreement, other than such vertical agreement as the Minister may by order specify. Singapore follows 'allowed unless specifically prohibited by order' approach as opposed to the 'prohibited'[27] and 'prohibited unless allowed because of efficiency consideration'[28] approach. The probable explanation for following such an approach is that rule of reason analysis is quite a costly exercise and lack of information to analyse any such agreement might lead to false positives and false negatives. Therefore, Singapore's competition authority finds it better to focus on whether firms with considerable market power can engage in successful exclusionary practices rather than proscribing vertical conduct in the first place.

Resale price maintenance agreement has often been accused of being anticompetitive as it destroys the intra-brand price competition among the retailers. By fixing the minimum floor price that can be charged from the ultimate consumer, it bereaves the consumers from the possibility of a potential price reduction at the retailers' level. This argument, though seems to be a strong advocate of banning RPM, is flawed by its necessary assumption. The argument assumes that intra-brand price competition[29] at the retailers' level is welfare enhancing. Next part of the paper will controvert this assumption and explain how intra brand price competition diminishes consumer welfare and should, therefore, be discouraged.

3. INTRA-BRAND PRICE COMPETITION: A CRITICAL ENQUIRY INTO ITS PROBABLE EFFECTS

Competition Law aims at ensuring 'productive efficiency'[30] and guaranteeing that a firm has an incentive to find newer and better ways of reducing cost. European Commission stated that the purpose of competition law 'is the protection of competition on the market as a means of enhancing consumer welfare and of ensuring an efficient allocation of resources'.[31] This makes it undoubtedly clear that the protection of competition is a means to meet the 'greater end' which is 'Consumer Welfare Maximization'. Two important observations flows from the preceding statement – firstly, competition law seeks to protect competition and not only 'price' competition and secondly, as long as the protection of competition is not leading to welfare maximization, there should be a room for deviation.

The following sub-parts will shed light on the problems that emerge as a result of outlawing the imposition of minimum RPMs and also the justifications for proposed reversal of that approach.

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[26] Section 34 of the Singapore's Competition Act prohibits anti-competitive agreements. See, Clause 4.1 of the CCS Guidelines on the Section 34 Prohibition, available at http://app.ccs.gov.sg/cms/user_documents/main/pdf/S34_Jul07FINAL.pdf. Also see Third Schedule to Competition Act, 2004 available at http://statutes.agc.gov.sg/non_version/cgi-bin/cgi_legdisp.pl?actno=2004-ACT-46-N&doctitle=COMPETITION%20ACT%202004.

[27] 'Per se' approach followed in Canada, Australia and EU.

[28] Rule of reason approach followed in US (after *Leegin's* case decided in 2007) and India.

[29] Intra-brand price competition is the competition among retailers for the price of the same product.

[30] Also 'allocative efficiency and 'dynamic efficiency.

[31] *Economic Foundations of Competition Law*, Asian Development Bank Toolkit, available at http:/www.adb.org/Documents/others/OGC_Toolkits/Competition-Law/documents/Chap1.pdf.

3.1. Free Rider Problem

This part of the paper will focus on how free rider problem transpires in situations where minimum RPM is not legally allowed. Production efficiency occurs when the firms seek to achieve the goal of producing goods at the minimum possible cost of production and they have an incentive to find newer ways to reduce costs as far as possible to earn maximum possible profits.[32] It is incontestable that the manufacturers' sales and profits are inversely related to the price of the product,[33] i.e. lower the price at which the distributors resell the products to the consumers, the greater will be the demand for the product and the profits will also increase accordingly.[34] Therefore, the manufacturer's desire to eliminate the intra brand price competition by imposing a minimum RPM cannot be but with a strong commercial justification. Lester G. Telser[35] has beautifully explained why a manufacturer is motivated to impose minimum resale price when 'he'[36] himself will benefit the most if the price of the product is kept at a minimum.[37] This raises an important question – what is the role of retailers in the process of production of goods? Why the manufacturer wants to regulate the retailers' activities by imposing a minimum resale price?

Indisputably, the retailer is not contributing towards the production of the goods in literal sense of the words. He is a producer of services (distribution) and facilitates the sale of goods produced by the manufacturer. However, in the absence of RPM, the retailer (who is not producing the product but only selling the product which is produced by the manufacturer) is competing on the price of the product when actually he has no control over its cost of production at the manufacturer's level. So the reduction in price which reaches the consumer is not because the retailers have become efficient or they have a lower cost of procuring the products, but because they have cut down on the services they were offering before. Although this might makes the product more attractive in terms of price, it will take away the services which the consumer finds useful and for which he is willing to pay.

Chicago School[38] of thought emphasizes that discounted dealers, who appear to benefit the consumer in the short run by providing products at cheaper prices, are in fact renegade free riders[39] who, if go unchecked, will destroy the supplier's place in the inter-brand market and ultimately decrease consumer choices.[40] Lester G. Telser, in 1960, provided the possible justification for imposing minimum resale price mechanism by emphasizing on the free riding problem. Telser opined that no frills distributors might 'free ride' on the promotional efforts

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[32] *Economic Foundations of Competition Law*, Asian Development Bank Toolkit, available at http:/www.adb.org/Documents/others/OGC_Toolkits/Competition-Law/documents/Chap1.pdf.

[33] For the purpose of this article, monopoly market model has not been considered; otherwise the results of situations considered will lead to variant consequences.

[34] Lester G. Telser (1960) 'Why Should Manufacturers Want Fair Trade?', 3 *Journal of Law and Economics*, 86-105 (1960).

[35] An American Economist and Professor Emeritus in Economics at the University of Chicago.

[36] 'He', wherever used in this article, is intended to be a gender neutral term implying 'he/she'.

[37] Lester G. Telser (1960) 'Why Should Manufacturers Want Fair Trade?', 3 *Journal of Law and Economics* 86.

[38] See generally, Richard A. Posner (1079) 'The Chicago School of Antitrust Analysis', 127(4) *University of Pennsylvania Law Review*, 925-48.

[39] Free Rider is a situation commonly arising in public goods context in which players may benefit from the actions of others without contributing (they may free ride).

[40] Jean Wegman Burns (2006) 'Challenging the Chicago School on Vertical Restraints', in *Utah Law Review* 913, *available at* http://privateweb.law.utah.edu/_webfiles/ULRarticles/69/69.pdf.

of full service distributors, thereby undermining the incentives of full service dealers to expend resources on promotion.[41] Thus, each person has an incentive to allow others to pay for the public good and not personally contribute. In short, the free rider problem occurs because one does not have an incentive to account for the global benefits of a private act.[42] Therefore, in the absence of minimum RPM, some retailers have the incentive to free ride on the services provided by the other retailers and, thereby, provide his own products at a lower price. This may sound a perfectly alright situation from a consumer point of view because as long as the consumer is benefitting from availing free pre-sale services from one retailer and buying from another at a cheaper price, he will attain greater consumer welfare. However, the author believes that this attractive strategy will survive only in the short run because in the long run no retailer will have an incentive to provide pre-sale services without any prospects of having a consumer demand for the products he is selling. This is explained in detail in the section dealing with game theory analysis of free riding problem.

3.2. Pre-Sale Services Justification

This part of the paper explicates how imposition of minimum RPMs on the retailers incentivizes them to provide useful pre-sale services. In the absence of an RPM agreement, the motivation to provide pre-sale services, if not altogether missing, is minimal. If the retailers choose to provide pre-sale services like expert pre-sale assistance on the product information, trial usage of the product etc., the cost of such services will accelerate the cost of the product to the final consumers. The problem arises when some retailers provide and some do not provide the important product specific pre-sale services. The consumer can go to the former retailer, see the product and avail all the pre-sale services which are free of cost and buy the product from the latter retailer at a discounted price. The latter retailer can give heavy discounts because he is not incurring any cost on providing pre sale services. RPM solves this free riding problem by making retail prices uniform, so that consumers no longer have a reason to shop from one store and buy from another. With no possibility to compete with each other on the basis of price, retailers that operate under RPM conditions will focus on non-price factors, i.e., services.[43]

The problem happens in the absence of RPM agreement, at least in case of some goods,[44] where consumer needs some pre-sale services before making an informed decision for buying a product. The kind of product market a consumer is facing today, presenting a wide array of differentiated products with specialized features and functions of every product, information regarding the functions and usage of a particular product becomes very important. A consumer buying an automobile, for example, will like to have a test drive and a consumer

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[41] Lester G. Telser, *Why Should Manufacturers Want Fair Trade?*, 3 Journal of Law and Economics 91(1960).

[42] Shor, Mikhael, *Free Rider,* Dictionary of Game Theory Terms, Game Theory.net, available at http://www.gametheory.net/dictionary/FreeRiderProblem.html (Web accessed: 24 September 2010).

[43] OECD Policy Roundtables, *Resale Price Maintenance*, DAF/COMP(2008) 37, *available at* http://www.oecd.org/dataoecd/35/7/1920261.pdf

[44] Here a distinction can be made between experience goods and search goods, as the latter will not require much of pre-sale service while the former will. An example of search good can be cotton, pencils, pens etc where consumer do not require much information or pre sale service to make a right choice. This, however, is not the case with experience goods where the absence of pre-sale services can lead the consumer to make a wrong choice.

buying cosmetics will like to have a free application test. There are various other product categories falling in this category, namely perfumes, electronic items, mobile phones etc. In such product markets, demand is the function of product features and quality as well as the price of the product.[45] Therefore, to know those product specific features, consumers need pre-sale services. But the problem is that, in the absence of minimum RPM, the retailers compete with each other on the price at which they offer the products to the final consumer. In the effort of attracting consumer, the retailers may bring down the price further and further to make 'their' product seemingly more economical. The dilemma here is that whether such a price war at the retailers' level is welfare maximizing? Whether 'intra-brand price competition' should be motivated?

The author is of the opinion that such intra-brand price competition is not only illusory but is also welfare diminishing because it might disincentivize the full service retailer to offer the important retail services that he was offering before. It will not only adversely affect the manufacturer but also the consumer. On the one hand, the manufacturer may be harmed because the product will not be able to capture the demand (at least that part of the demand which is directly proportional to the pre-sale services) in the absence of pre-sale services. On the other hand, the consumer will make lesser informed choices and they might end up making a wrong decision thereby resulting in diminished consumer welfare. However, by imposing minimum resale price restraint, a manufacturer can eliminate the unnecessary intra-brand price competition which in turn encourages retailers to invest in tangible or intangible services or promotional efforts that aid the manufacturer's position as against rival manufacturers.[46]

This can be explained by taking an example. Suppose the manufacturer deal in product 'x' which is an experience good (which generally requires a consumer to use/experience the product before buying) e.g. a Perfume. He sells the product to the retailers at a price of USD 100. It is true for a rational consumer to first experience the product (Perfume) before making a decision whether to buy or not to buy the product. **Scenario 1** – RPM is illegal and therefore, not imposed: In the absence of RPM, the dealers will compete on price and charge as low as USD 101 or may be even USD 100 to capture consumer demand. In order to avoid losses, a rational dealer will not provide any pre-sale service. In the short run, free riding (as explained above) will take place and in the long run, all retailers will stop providing pre sale service. The result will be two fold – the consumers will be bereft of necessary information to make an informed decision and the demand for manufacturers' product will be adversely affected. Contrasted to this is another situation as will be stated below.

Scenario 2 – RPM is not illegal and therefore, is imposed: In the presence of minimum RPM imposed by the manufacturer (suppose USD 110 is the minimum resale price), the dealer cannot compete anymore on price as all will be selling at either USD 110 or above. In such a situation the only way they can capture consumer demand is by providing useful

[45] Kenneth G. Elzinga and David E. Mills (2010) 'Leegin and Procompetitive Resale Price Maintenance', 55 (2) *The Antitrust Bulletin* 349.
[46] *Leegin Creative Leather Products, Inc., v. PSKS, Inc.*, 127 S.Ct. 2705 (2007).

services. The margin of USD 10 is available with every dealer to utilize it as efficiently as possible. Since they cannot sell below USD 110, only way they can attract consumers is by competing on the services. This will motivate the dealer to provide the services efficiently to bring down the cost of producing services and thereby increase his profit from that margin. It will not only take away the intra-brand price competition but also instigate intra-brand non-price competition, which is the required outcome.

Some scholars argue that minimum RPM provides too much liberty to the manufacturer to impose the minimum price at which the product should be sold and thereby deprives the consumers of the benefits of price competition among retailers. This argument doesn't stand good, unless the manufacturer is a dominant player in the market and he is abusing his dominant position to dictate the product's price. And if that is the case, then there is an altogether different provision in competition law in every jurisdiction to deal with such a situation – provisions relating to '*Abuse of Dominant Position*' (In US, the provision is termed as '*Monopolization*').

It should be noted here that the minimum RPM of USD 110 cannot be an arbitrary figure because every manufacturer is incentivized to keep the price as minimum as possible. Law of demand will operate to ensure that – lower the price, more will be the demand for manufactures' products. Therefore, the minimum RPM will be decided by the manufacturer by keeping in consideration the optimum amount of pre-sale services required to build and maintain the demand for his particular product and the price of other competitive products in the market. Inferentially, inter-brand price competition will ensure that the manufacturer is not keeping the RPM towards the higher side to exploit the consumers. Inevitably, these opposite forces will keep a check on the minimum RPM fixed by the manufacturer. A different result will follow when the manufacturer has a dominant position in the market and can keep a price (resale price) irrespective of what the other actors in the market are charging. However, this situation can be corrected by invoking the provisions of 'abuse of dominant position' present in all competition law statutes in different countries.

In this high tech world featured with uncertain demand, the absence of pre-sale services may also lead to inadequate supply in the market. Various economic researches support the hypothesis that uniform pricing can support larger inventories and sales of manufacturer's products, and in so doing provides a new explanation for manufacturer willingness to impose RPM.[47] Therefore, a ban on RPM under the competition law regime will instigate the manufacturer to informally bring a uniform price in the market for his product using alternate tactics. An example of this can be State of Maryland, where strong ban on minimum RPM through legislation was ineffective in bringing intra-brand price competition among retailers. It is quite interesting that after the US Supreme Court legitimized rule of reason approach in case of resale price maintenance agreements in Leegin's case overturning the 100 year per se standard of Dr Miles case, many states considered legislation as a means to circumvent

[47] Raymond Deneckere, Howard P. Marvel and James Peck (1996) 'Demand Uncertainty, Inventories, and Resale Price Maintenance', 3(111) *The Quarterly Journal of Economics*, 885-913, *available at* http://www.econ.ohio-state.edu/pdf/niche.pdf.

Leegin, one of which was State of Maryland. The economist, analysing the effect of RPM on retail prices in the video games industry, could not find much evidence that Maryland statute had any effect on video game prices. The probable reason for no effect of banning RPM statutorily was that manufacturers were able to use other tools that result in the manufacturer achieving the same retail pricing practices as minimum RPM. The economists, however, further concluded that the total welfare will go down if the suppliers are forced to substitute RPM by less efficient means to achieve the same results.[48]

3.3. Game Theory Analysis

The free riding problem in the market at the distributors' (retailers') level and its consequences can be explained by using prisoners' dilemma analysis. The game theory analysis of this part is located and is tested, hypothetically, in a jurisdiction where minimum RPM is not allowed under the competition law.

Assumptions:

(1) R_1 and R_2 are rational market players;
(2) Minimum RPM is prohibited under the Competition Law;
(3) They are the only two retailers distributing a manufacturer's product X;
(4) Product X is not a necessary product, meaning that the demand is price elastic and law of demand is appliable;
(5) Retailers procure one unit of X from the manufacturer at the cost of Y;
(6) The total demand of product X in the market is D and both retailer keep enough inventory to meet the demand individually;
(7) Pre-sale services, which are product specific and indispensible for sale, costs α per unit and $D\alpha$ in total;
(8) The profit margin which the retailers (R1 and R2) wish to make is p (it is, therefore, the difference between the selling price and cost price of X);
(9) $p > \alpha$, for any market situation

Table 1: Showing the structured payoffs for R_1 and R_2 in different situations

	R_1 provides pre-sale services	R_1 does not provides pre-sale services
R_2 provides pre-sale services	$((Dp-D\alpha)/2 , (Dp-D\alpha)/2)$	$(Dp, -D\alpha)$
R_2 does not provides pre-sale services	$(-D\alpha, Dp)$	$(0, 0)$[49]

[48] Elizabeth M. Bailey and Gregory K. Leonard (2010) 'Minimum Resale Price Maintenance: Some Empirical Evidence from Maryland', in 10(1) *The B.E. Journal of Economic Analysis & Policy* (2010), *available at:* http://www. bepress.com/bejeap/vol10/iss1/art17.

[49] This is an extreme situation where the consumer will not buy the product at all because of absence of pre-sale services in the market. Another extreme situation occurs when both R_1 and R_2 will share the market demand equally, in which case their respective payoffs will be Dp/2. This will not happen because it has been assumed that Product X is not an essential commodity and pre-sale services are indispensable. In reality, therefore, the payoffs for both R_1 and R_2 will lie somewhere between 0 and Dp/2.

Considering the presumptions stated above, both the retailers R_1 and R_2 have the incentive to breach the obligation of providing pre-sale services to the consumer because if one of them provides and the other does not provide, the one providing will lose $D\alpha$ and the one who is not providing will grab the total demand in the economy thereby earning the profit Dp. If both of them provide the pre-sale service they will both share the market demand which will be D/2 and they will both share the profit and equally incur the cost ($D\alpha/2$). So their pay offs in that case will be $(Dp-D\alpha)/2$. But in the absence of such understanding where both of them provide resale services, R_1 and R_2 have no incentive to provide pre sale service because each one will be scared of the other retailer's behaviour and will act presuming that the other will not provide the pre-sale service. This will result in complete extinction of pre-sale services from the market for a particular product making it undesirable by the consumers, who cannot evaluate the products except by risking their money in it. A rational consumer will probably choose not to purchase the product instead of making a wrong and arbitrary decision. Even taking the other extreme that the consumers will still buy the product – there will be a net negative welfare in the society if more than half of them make a wrong decision pursuant to absence of information on the product usage and utility. The payoffs of R_1 and R_2 in this scenario will lie between 0 and Dp/2.

The situation would have been different if RPM was allowed. When the manufacturer fixes the minimum RPM in the market, the retailer can no more compete on the price. Therefore, the retailers will compete with each other for the sales by offering valuable retail service to consumers.[50]

4. COMPETITION LAW, INTERNATIONAL TRADE AND RESALE PRICE MAINTENANCE AGREEMENTS – DEVELOPMENTS AND CHALLENGES AHEAD

With the growing trade and commerce interaction between nations, the present discussion will be incomplete without a mention of international developments on the issue of cooperation and convergence of competition law principles. Today more than 100 countries have enacted their respective competition laws and many others are in the process of enacting.[51] Though the competition law principles entrenched in respective countries' statutes are more or less similar, there is no single binding international document or forum that is applicable to all nations.[52] There have been some unanimous opinions on internationally accepted best practices but there is no 'multilateral agreement on competition', in spite of the talks regarding the adoption of the same. A case for multilateral agreement on competition was made at WTO as early as at the Havana Charter which was signed in 1948.[53] However, the

[50] Kenneth G. Elzinga and David E. Mills (2010) 'Leegin and Procompetitive Resale Price Maintenance', 55 (2) *The Antitrust Bulletin* 349.
[51] Asian Development Bank, Competition Law Toolkit (2007) available at http://www.adb.org/Documents/Others/OGC-Toolkits/Competition-Law/complaw030000.asp.
[52] Andrew T. Guzman and Alan O. Sykes (2007) *Research Handbook in International Economic Law*, 418 (Edward Elgar Publications)
[53] Francisco Gonzalez de Cossio, International Aspects of Competition Law, available at http://gdca.com.mx/PDF/competencia/INTERNATIONAL%20ASPECTS%20COMPETITION%20LAW.pdf

serious attempts to make it a reality were propelled at the Singapore Ministerial Conference in 1996 where a working group was set up to study issues on the interaction between Trade and Competition Policy.[54] It was not long before the working group was rendered inactive in 2004 and it was decided that issue of competition policy will not form part of the Work Programme set out in that Declaration. There is still a debate in the international community on whether the international norms or binding rules on competition should form part of the WTO agreement or not. Any view in favour of including competition law within the WTO must be based on the clear understanding on what should be considered – in terms of rules and principles – in those further negotiations. Whether there should be a set of comprehensive competition rules extending beyond the core prohibition on cartels and serious abuses of dominance to business phenomena such as mergers or vertical restraints; whether these rules should be subject to dispute settlement procedures, whether the rules should operate within the prevailing WTO principles such as transparency, national treatment and non-discrimination; whether specialized contextualized approach to competition law should be designed – are some of the questions that need concrete answers before the case in favour of WTO as a forum for international competition law is considered.[55] It is true that the competition law (operating at domestic levels) is in a way miniature form of international trade law. Like international trade, competition law also aims at achieving fair trade; even competition law seeks to prohibit distortionary trade practices; and even competition law worries about protectionist measures. But there remain certain differences e.g. some national competition laws allow export cartel even when cartel within their domestic markets are prohibited,[56] some national competition laws aim at securing consumer welfare[57] while some others may aim at different objects like market economic integration,[58] Therefore, different economic developments demand different objectives to be fulfilled and this is probably the reason why one competition law may not be acceptable to all economies. Arguably, however, this should not present a problem provided that market access hindrances are considered from a shared perspective, competition and trade policy.[59]

The major issue that needs to be considered in this scenario is whether we really need a multilateral agreement to be enforced through a forum like WTO when most countries presently have their distinct domestic competition law in place? Would it be right in such a scenario to have 'one-size-fit-all' type of agreement on competition? The US has been highly sceptical about the appropriateness of WTO as a forum for negotiating competition rules.[60] The EU, however, has been in favour of internationalization of competition rules; though even EU has shown scepticism about converging substantive provisions of the competition laws of different countries which can only happen with the passage of time.[61] European

[54] Maher M. Dabbah (2010) *International and Comparative Competition Law*, (Cambridge: Cambridge University Press) 551.
[55] Maher M. Dabbah (2010) *International and Comparative Competition Law*, 551-552.
[56] See Indian Competition Act, 2002, Section 3(5)(ii).
[57] US antitrust law aim at securing consumer interest as the main objective.
[58] EC has the main objective of market integration of the EU states.
[59] Maher M. Dabbah (2010) *International and Comparative Competition Law*, 594.
[60] Maher M. Dabbah (2010) *International and Comparative Competition Law*, 556.
[61] Maher M. Dabbah (2010) *International and Comparative Competition Law*, 558.

Commission has suggested a step-by-step approach to begin with preliminary negotiations focusing at ensuring adequate and transparent competition law enforcement in different jurisdictions, building international cooperation through exchange of non-confidential information and through incorporating notification and positive comity[62] provisions.[63]

Therefore, considering the challenges that exist in adopting a multilateral agreement on competition, i.e. different forms and different goals of competition law in different countries and different understanding of the word 'competition' in different jurisdictions suggest convergence through non-binding commitments. Convergence and harmonization, at procedural and substantive level, have taken place in the past by international bodies and organization such as UNCTAD, the OECD and the ICN.

The UNCTAD promotes cooperation and convergence of national competition policies through consultation and information-sharing. Established in 1964, UNCTAD serves as a forum for intergovernmental deliberations among its 192 members and provides research, policy analysis and data collection, and technical assistance tailored to the specific requirements of developing countries.[64] UNCTAD has addressed the trade-competition linkage by formulating a host of initiatives to address restrictive business practices and competition policy, including voluntary codes, handbooks, and even a Model Law on Competition to assist countries drafting competition laws for the first time.[65] One of the most prominent initiatives among its competition-related initiatives are the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices which were released in 1980, and have been reviewed four times in 1985, 1990, 1995 and 2000.[66] It was affirmed in the rules that 'a set of multilaterally agreed equitable principles and rules for the control of restrictive business practices can contribute to attaining the objective in the establishment of a new international economic order to eliminate restrictive business practices adversely affecting international trade and thereby contribute to development and improvement of international economic relations on a just and equitable basis'.[67] UNCTAD focuses much energy on technical assistance and capacity-building for developing countries

[62] Though not defined anywhere as such, positive comity implies a kind of co-operation (mostly in international cases e.g. denial of market access) between country's whereby one country requests the other to conduct law enforcement proceedings against a practice in latter's territory which is affecting the former country. Such co-operation has immense potential in laying down the foundational stones for any prospective internationalization of competition law rules.

[63] Maher M. Dabbah (2010) *International and Comparative Competition Law*, 558.

[64] Chad Damro (2005) 'Discretionary Cooperation and the Regulation of Internationalizing Business Activity', Paper prepared for the Third ECPR General Conference Budapest, Hungary, available at http://regulation.upf.edu/ecpr-05-papers/cdamro.pdf.

[65] UNCTAD, Capacity-building on competition law and policy for development, A Consolidated Report (2008), available at http://www.unctad.org/en/docs/ditcclp20077_en.pdf.

[66] Chad Damro (2005) 'Discretionary Cooperation and the Regulation of Internationalizing Business Activity', Paper prepared for the Third ECPR General Conference Budapest, Hungary, available at http://regulation.upf.edu/ecpr-05-papers/cdamro.pdf.

[67] Competition and Consumer Policies, *The Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices*, available at http://r0.unctad.org/en/subsites/cpolicy/docs/CPSet/cpsetp4.htm.

that are establishing competition law and policy. In this regard, UNCTAD cooperates with the OECD, WTO and ICN.[68]

OECD have also been playing a pro-active role in publishing recommendations and best practices in the field of competition law e.g. 'Guidelines for fighting bid-rigging in public procurement (2009)', 'Recommendation on competition assessment (2009)', 'Best Practices for the formal exchange of information between competition authorities in hardcore cartel investigations (2005)', 'Recommendation of the council concerning cooperation between member countries on anticompetitive practices affecting international trade (1995)' etc. through its ground-breaking output, the OECD has maintained the goal of achieving a variety of benefits for competition authorities, firms and consumers in different OECD countries and to some extent non-OECD countries.[69]

ICN is different from other international bodies in the sense of being a virtual network, though this body has worked tremendously towards ensuring cooperation between national competition authorities. ICN is working only on competition issues and it emphasizes on consensus building which may go a long way in achieving the pursuit of multilateralism through non-binding commitments in the field.[70] ICN has membership of around 114 members comprising of national competition authorities of different countries.[71] Because of its greater emphasis on consensus it has achieved both credibility and popularity among different nations – both developed and developing.[72] ICN has worked on number of important issues concerning international community e.g. 'conflict of jurisdiction principles', 'merger notification principles', 'merger review period principles', notification form principles', 'merger remedies principles, 'procedural principles' etc.[73]

Resale Price Maintenance is one of the competition law issues which has received different treatment in most nations – some prohibit it *per se*,[74] some evaluate it under rule of reason[75] and others consider it as pro-competitive unless abuse of dominant position is involved.[76] Therefore, how various jurisdictions will deal with this issue at the international level seems to be a challenge. This paper pitches in favour of RPM agreements by providing economic and commercial justifications and, therefore, suggests that consensus of different states on this point can be aimed at. The international organizations can work towards bringing the international community on a unanimous note by highlighting the justifications on RPM agreements. This will not only lead to lower administrative costs in countries that

[68] Chad Damro (2005) 'Discretionary Cooperation and the Regulation of Internationalizing Business Activity', Paper prepared for the Third ECPR General Conference Budapest, Hungary, available at http://regulation.upf.edu/ecpr-05-papers/cdamro.pdf.
[69] Maher M. Dabbah (2010) *International and Comparative Competition Law*, 138.
[70] R. Hewitt Pate , Building Consensus: The International Competition Network's Merger Review Working Group, Second Annual International Competition Network Conference Merida, Mexico (2003), available at http:// www.justice.gov/atr/public/speeches/209658.pdf.
[71] Hugh M. Hollman and William E. Kovacic, *The International Competition Network: Its Past, Current and Future Role*, 20(2) Minnesota Journal Of International Law 275 (2011), available at http://www.ftc.gov/ speeches/kovacic/1106internationalcompnetwork.pdf.
[72] Maher M. Dabbah (2010) *International and Comparative Competition Law*, 573.
[73] Maher M. Dabbah (2010) *International and Comparative Competition Law*, 152.
[74] Canada, Australia etc. Even US imposed a *per se* standard of evaluation till 2007.
[75] US, India etc.
[76] Singapore etc.

end up spending high figures on investigating RPM practices, but will also bring the focus towards more pernicious practices like cartels, other horizontal collusions and abuse of dominant position.

5. CONCLUSION

This paper argues in favour of 'Resale Price Maintenance' agreements and exemplifies how the myth of RPM being anti-competitive is wrongly founded and premised. Forgoing analysis provides logic to the postulation that minimum RPM agreements, though traditionally held to be anti-competitive, actually leads to higher consumer welfare. It is quite apparent that a ban on resale price maintenance agreement not only allows the burgeoning of illusory *intra-brand price competition* among the retailers but also demotivates the manufacturer to produce innovative products which can enhance consumer utility and surplus. Besides creating an artificial demand-supply mismatch in the market, the ban might also limit consumer choices, thereby prompting the consumer to take an ill informed decision which will further result in a welfare loss. By lifting the ban from minimum resale price maintenance agreements, the regulators can actually motivate the retailers to provide product specific services, which help in eliminating *intra-brand price competition* and building the demand for certain products, are of vital value not only to the consumers but also to the manufacturer. The elimination of *intra-brand price competition* serves twin objectives – firstly, it stimulates *intra-brand non-price competition* and, secondly it also inspires *inter-brand price competition.* Though, presently the competition authorities in most countries (e.g. U.S., India and UK) apply less strict standards while dealing with minimum RPMs but nevertheless, the conduct is still within the ambit of anti-competitive agreements under the competition laws of those jurisdictions. And in order to pull those agreements out of the subjugation of competition law provisions, it is necessary to prove that the pro-competitive effects of such agreements supersede the anti-competitive effects. This not only imposes cost on the business actors but also hamper the free-flowing of business operations. Therefore, it is advisable to adopt a positive approach in case of such practices – i.e. unilateral imposition of minimum RPMs by a manufacturer (supplier) should be allowed unless abuse of dominance could be proved on his part or unless the imposition of minimum RPMs is the result of coercive tactics employed by the retailers on the manufacturer (supplier). As is already explained earlier that the former can be dealt under provisions relating to '*Abuse of Dominance Position*'[77] and the latter can be dealt under provisions relating to '*Collusion*'. Therefore, there is a need to adopt a shift in the approach to save administrative costs and resulting false positives[78].

[77] '*Monopolization*' if referring to the US Sherman Antitrust Act, 1890.

[78] False positive is a judgmental/testing error that may take place when the competition authorities end up penalizing a welfare enhancing minimum RPM agreement.

It is interesting to note the observation made by an American judge, as early as in 1911[79] while dissenting from the other learned judges, expressing his apprehension on the prohibition on minimum retail price mechanism:

> I cannot believe that, in the long run, the public will profit by this Court's permitting knaves to cut reasonable prices for some ulterior purpose of their own, and thus to impair, if not to destroy, the production and sale of articles which it is assumed to be desirable that the public should be able to get.[80]

[79] At that time, the minimum RPMs were held to be 'per se' violation under the Antitrust Act in the US. To be more precise, U.S. has evolved the per se and rule of reason approach through case laws. The issue relating to the legality or legitimacy of minimum resale price maintenance agreement came before the Court in this particular decision, *Dr. Miles* case; where the court (majority) held that minimum resale price maintenance agreements fall under the category of 'per se' violation.

[80] Justice Oliver Wendell Holmes, Jr., dissenting in *Dr. Miles Medical Co., v. John D.Park & Sons Co.*, 220 U.S.409 (1911).