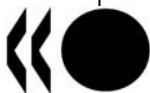


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DAF/COMP(2008)37



Organisation de Coopération et de Développement Économiques
Organisation for Economic Co-operation and Development

10-Sep-2009

English, French

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

**DAF/COMP(2008)37
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ROUNDTABLE ON RESALE PRICE MAINTENANCE

JT03269395

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GERMANY

1. Legal Background and Definition of Resale Price Maintenance (RPM)

Since the amendment to the German Act against Restraints of Competition (ARC)¹ in 2005, § 1 ARC contains a general clause which mirrors Article 81 (1) EC. The provision bans “agreements between undertakings, decisions by associations of undertakings and concerted practices, which have as their object or effect the prevention, restriction or distortion of competition.” Resale price maintenance (RPM) also falls under this definition. Consequently, in Germany both Article 81 (1) EC and § 1 ARC apply to RPM. It follows that Article 81 (3) EC and the corresponding § 2 ARC are applicable as well, which exempt such an agreement “which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not: (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives; [and] (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question”. Further to this, § 30 ARC provides for an exemption from the general RPM prohibition for books, newspapers and magazines².

The ARC, in its present form, does not contain a definition as to what is considered to be RPM. However, § 14 of the ARC(old) which specifically prohibited RPM can still be used as a definition. It banned any “agreements between undertakings which [...] restrict a party in its freedom to determine prices ... in agreements which it concludes with third parties on the goods supplied, on other goods, or on commercial services.” This broad definition is only narrowed insofar as the setting of maximum resale prices is now accepted in Article 4 lit. a of the EC Commission’s Regulation on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices (No 2790/1999)³.

2. RPM in the Bundeskartellamt’s experience

In the experience of the Bundeskartellamt, as regards the pricing of products, an important concern for producers is downward pressure on prices at the retail level. In that respect, e-mail or other correspondence by producers telling resellers that they are selling a high quality product which must therefore not be sold at low prices is not uncommon. Producers seem to be afraid that a general erosion of prices charged to the final consumer will ultimately lead to retailers bargaining harder and demanding lower prices from their suppliers. One objective of producers therefore is to secure stable (high) prices. Consequently, RPM has been criticised as potentially weakening the productivity pressure on the producer’s margin⁴.

¹ An English version of the ARC is available at http://www.bundeskartellamt.de/wEnglisch/download/pdf/06_GWB_7__Novelle_e.pdf.

² The Bundeskartellamt has not as yet been able to assess whether this has led to positive effects that can be measured in competition terms.

³ The Regulation is available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:1999:336:0021:0025:EN:PDF>.

⁴ See Peeperkorn, *Resale price maintenance and its alleged efficiencies*, European Competition Journal (2007), p. 201 *et seq.*, p 207 *et seq.*

From the retailer's perspective, it deserves mention that some retailers shy away from price competition at the retail level. Thus, manufacturers are often lobbied by dealers to enforce minimum price levels.

The Bundeskartellamt receives complaints about fixed resale prices from both retailers and end customers. While the former are prevented from boosting their sales through price cuts, the latter complain that they have been unable to obtain discounts from dealers.

RPM is often imposed "across the board", regardless of whether a product is technically sophisticated or easy to use⁵. The service argument, *i.e.* the argument that a uniform price level is needed to ensure proper customer service and advice and to avoid free-riding (see below), thus often seems to be a pretext to use RPM to restrain the freedom of setting prices in vertical business relations. So far, the Bundeskartellamt has not been confronted with any case where a company has credibly brought forward an efficiency defence on the grounds that RPM was indispensable to generate pro-competitive effects. Rather, less restraining measures such as exclusive distribution, price recommendations and the setting of maximum prices would have been sufficient.

3. Competitive Effects of RPM

3.1 Positive effects of RPM – Avoid free-riding

The primary argument in favour of fixed resale prices is that free-riding can be avoided⁶. Resale price maintenance guarantees the seller a certain profit margin on the product sold. This encourages him to concentrate his sales efforts on a particular product. In the same vein, RPM allows sellers to provide better services to consumers such as better advice and product explanations. Conversely, RPM prevents other distributors or sellers from benefiting from promotion efforts made by rivals. Without resale price maintenance the following might happen: Seller A is heavily investing in advertising a certain product or providing costly additional service to customers. Seller B who is located nearby makes no such investment. As he has not incurred promotional costs seller B may now be able to sell the product cheaper than seller A, thus free-riding on A's efforts. The problem may also arise where seller A operates a physical store whereas seller B only sells goods over the internet.

However, a seller may not use the extra profits guaranteed through RPM to invest them in promotion after all. Such guaranteed extra profits cannot be considered to provide a sufficient incentive to actually spend the extra money on promotion⁷. Instead, the seller may stick with all or some of the extra profits rather than investing in promotion, possibly still free-riding on other sellers' promotional efforts. Consequently, the problem of free-riding is not solved.

The majority opinion in the *Leegin* case furthermore argued that RPM may be useful for new entrants to a market⁸. By ensuring resellers a high profit margin the latter will be encouraged to sell the product

⁵ See Tirole, *The Theory of Industrial Organization*, Cambridge, Massachusetts, 1988, p. 183.

⁶ Peeperkorn, *Resale price maintenance and its alleged efficiencies*, European Competition Journal (2007), p. 201 et seq, p. 208 et seq. See also Tirole, *The Theory of Industrial Organization*, Cambridge, Massachusetts, 1988, p. 183; Motta, *Competition Policy*, Cambridge, 2004, p. 313. See also *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U. S. (2007), Opinion of the Court, p. 11, available at <http://www.supremecourtus.gov/opinions/06pdf/06-480.pdf>.

⁷ Peeperkorn, *Resale price maintenance and its alleged efficiencies*, European Competition Journal (2007), p. 201 et seq. p. 209.

⁸ See *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U. S. (2007), Opinion of the Court, p. 11, available at <http://www.supremecourtus.gov/opinions/06pdf/06-480.pdf>, p. 11.

with the higher profit margin rather than a competing product which may be less profitable for them. In such a scenario the uniform pricing would help to avoid an erosion in retail prices which could occur if resellers were competing on price. On the other hand, this is not an argument to allow RPM for a long period, or for established players and brands⁹. It is, *a fortiori*, also not an argument for establishing the rule that competition authorities should always bear the burden to prove the anticompetitive effects of RPM¹⁰.

The proponents of RPM concede that fixed resale prices will lead to uniform pricing vis-à-vis the final consumer. They claim, however, that this decrease in intra-brand competition is outweighed by the stimulation of inter-brand competition¹¹. The view that it is more important to protect and maintain competition between producers than to protect competition between distributors does not, however, give sufficient credit to intra-brand competition. Intra-brand competition is competition at the distributors' level, *i.e.* competition of the market level vis-à-vis the consumer. This competition at retail level – and consequently a consumer's possibility to choose the retailer with the mix of price and service that suits him or her best – should not be limited by competition laws or their application¹².

3.2 *Negative Effects of RPM – Lessening inter- and intra-brand competition*

Depending on the goods in question, the price may play a varying role. However, price is generally one of the essential criteria in the overwhelming majority of purchase decisions. This holds especially true where the end customer is concerned. Of course, manufacturers are free to sell their goods to distributors at a high price (and thereby achieve a high price level) *e.g.* if they consider that this contributes to a desired product image. However, it is difficult to see how restricting the *retailer's* freedom to set prices and thus keep them artificially high should yield any tangible benefits for the consumer.

Rather, prices can be expected to be higher since distributors are prevented from lowering their sales price for a particular product¹³. Since RPM eliminates intra-brand price competition at the retail level, any consumer wishing to buy a particular product of a certain brand cannot shop around for a good price but has to settle for the price imposed by the manufacturer. It is doubtful whether in practice inter-brand competition can work as an effective counterweight to the elimination of intra-brand price competition. Proponents of RPM argue that high price levels are discouraged due to inter-brand competition. However, branded products by their very nature are often differentiated, either technically or in terms of image. Inter-brand competition is thus already prevented to some extent from working as a corrective. What is more, competitors might not always be inclined to compete on price but instead prefer a non-offensive pricing environment supported and stabilised by RPM. On the other hand, there is the likelihood that fierce intra-brand competition will ultimately also boost inter-brand competition.

It also seems worth mentioning that when RPM is applied it will be unusual that price-cuts of producers vis-à-vis distributors are passed on to consumers since it is unlikely that in this event the fixed

⁹ See Peeperkorn, *Resale price maintenance and its alleged efficiencies*, European Competition Journal (2007), p. 201 *et seq.*, p. 211.

¹⁰ Cf. Schwaderer, *Eine Frage der Abwägung: Form- oder wirkungsbasierter Ansatz*, WuW (2008), p. 657.

¹¹ See, for instance, the FTC's and DOJ's Brief for United States as Amicus Curiae 6 (available at <http://www.ftc.gov/os/2007/01/070122Leegin06-480amicusPDC.pdf>), p. 10.

¹² See Peeperkorn, *Resale price maintenance and its alleged efficiencies*, European Competition Journal (2007), p. 201 *et seq.*, p. 207. Cf. also *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U. S. (2007), dissenting opinion (Justice Breyer), p. 4, available at <http://www.supremecourt.us/opinions/06pdf/06-480.pdf>.

¹³ Cf. Peeperkorn, *Resale price maintenance and its alleged efficiencies*, European Competition Journal (2007), p. 201 *et seq.*, p. 207.

retail price would be adjusted. Consequently, price-cutting is unlikely to generate any additional turnover in the product concerned.

Furthermore, RPM may facilitate collusion and stabilise cartels, in particular supply-side cartels¹⁴. Fixed prices at the retail level increase price transparency in a market. In this way, they facilitate the monitoring of cartel discipline. Moreover, they make it far less attractive to cheat on other cartel members. Especially in markets with few players, RPM may lead to price alignment at a certain level, given the greater price transparency in the market. The same effect may arise when recommended sales prices are used in a market. RPM would, however, considerably strengthen this effect.

4. Need for change in German and European competition law?

In the wake of the *Leegin* judgment, there are calls in Europe to stop regarding RPM as generally anticompetitive¹⁵ and introducing a rebuttable presumption in favour of its legality¹⁶.

The Bundeskartellamt is of the opinion that this would be a step in the wrong direction¹⁷. The above-mentioned arguments in favour of and against RPM show that RPM may generate efficiencies but also make it very clear that these efficiencies are often not sufficient to outweigh the severe restrictions in price competition which it causes. Consequently, jurisdictions have to weigh the risks and benefits and find solutions that are practical and manageable for competition agencies¹⁸.

In this respect it needs to be stressed that the approach towards RPM under the European and German rules differs considerably from the US *per se* approach that applied to RPM before the *Leegin* judgment. Under European law, it is presumed that RPM is anticompetitive. However, if companies come forward with evidence that a vertical agreement generates efficiencies that may fulfil the conditions of Article 81 (3) EC or § 2 ARC, the competition agency would have to make its case that the agreement is indeed anticompetitive¹⁹.

In view of the negative effects of RPM mentioned above, it does not seem justified to change this order of presenting evidence. More specifically, in the light of these effects, a (rebuttable) presumption in favour of RPM's legality would impose too heavy a burden on a competition agency or a plaintiff to

¹⁴ Motta, *Competition Policy*, Cambridge, 2004, p. 158, Peeperkorn, *Resale price maintenance and its alleged efficiencies*, European Competition Journal (2007), p. 201 *et seq.*, p. 206. Cf. also *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U. S. (2007), dissenting opinion (Justice Breyer), p. 4 *et seq.*, available at <http://www.supremecourtus.gov/opinions/06pdf/06-480.pdf>.

¹⁵ See Kneepkens, *Resale Price Maintenance: Economics Call for a More Balanced Approach*, ECLR (2007), p. 656 *et seq.*; Kasten, *Vertikale (Mindest-)Preisbindung im Licht des "more economic approach"*, WuW (2007), p. 994 *et seq.*; v. Weizsäcker, *Konsumentenwohlfahrt und Wettbewerbsfreiheit: Über den tieferen Sinn des "Economic Approach"*, WuW (2007), p. 1079; Orbach, *Antitrust vertical myopia – the allure of high prices*, Arizona Law Review 50 (2008), pp. 286 *et seq.*

¹⁶ See, for instance, Alesse, *Unmasking the masquerade of vertical price fixing*, ECLR (2007), pp. 514-526.

¹⁷ See also Schwaderer, *Eine Frage der Abwägung: Form- oder wirkungsbasierter Ansatz*, WuW (2008), p. 653 *et seq.* who argues that the majority vote in *Leegin* “does not yield any new empirical insights about how often the benefits or harm of vertical minimum price restraints actually occur. Thus, the majority should not cause Europe to change its approach.”

¹⁸ Cf. Justice Breyer, transcript of the hearing in the *Leegin* case, p. 18. The transcript is available at http://www.supremecourtus.gov/oral_arguments/argument_transcripts/06-480.pdf.

¹⁹ For a more detailed comparison see Peeperkorn, *Resale price maintenance and its alleged efficiencies*, European Competition Journal (2007), p. 201 *et seq.*, p. 203 *et seq.*

establish that a specific RPM system has anticompetitive effects²⁰. Furthermore, given the limited resources available, cases of RPM that may merit being taken up under competition law would probably not be investigated.

Moreover, a change does not seem justified since the alleged pro-competitive effects of RPM often do not materialise in the real world. What is more, such effects can mostly be achieved by measures that are less restrictive of competition. Consequently, the negative effects resulting from eliminating intra-brand competition are normally not outweighed by alleged pro-competitive effects.

The Bundeskartellamt is therefore of the opinion that the current rules under EC law (which are mirrored by German law) address the RPM issue in an appropriate manner. To successfully invoke an efficiency defence, the thresholds of Article 81(3) EC have to be met. The Bundeskartellamt is open to carefully reviewing any valid arguments in favour of RPM and to assessing whether very specific circumstances might make some form of RPM indispensable to achieve pro-competitive effects.

²⁰

See Schwaderer, *Eine Frage der Abwägung: Form- oder wirkungsbasierter Ansatz*, WuW (2008), p. 653 *et seq.*, 659 *et seq.* Cf. also Tirole, *The Theory of Industrial Organization*, Cambridge, Massachusetts, 1988, p. 186. Cf. also *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U. S. (2007), dissenting opinion (Justice Breyer), p. 9 *et seq.*, pointing out that it is not easy to “identify instances in which the benefits are likely to outweigh the potential harms”. The Slip Opinion is available at <http://www.supremecourtus.gov/opinions/06pdf/06-480.pdf>.

