ANTITRUST

WILL CORPORATE AMERICA SAY "WE'RE NOT IN KANSAS ANYMORE" AFTER THE KANSAS SUPREME COURT'S ANTITRUST DECISION IN *O'BRIEN V. LEEGIN*?

by James M. Burns and Adam M. Wenner

In 2007, the Supreme Court overturned almost one hundred years of settled antitrust precedent by declaring that retail price maintenance ("RPM"), the practice by which a manufacturer attempts to dictate the resale price of its products, was no longer *per se* unlawful under the federal antitrust laws. *Leegin Creative Leather Products v. PSKS Inc.*, 551 U.S. 877 (2007) ("*Leegin*"). Instead, RPM would be assessed under the "rule of reason," which, unlike the *per se* tested that declares such conduct unlawful in all circumstances, requires the Court to weigh the procompetitive justifications for the agreement against its anticompetitive effects in determining the legality of the conduct. In short, a balancing act similar to that used in assessing most other antitrust issues (other than horizontal price fixing and market allocation agreements) would apply to RPM agreements, opening the door -- or so it seemed -- for some manufacturers to exert greater control over retailer pricing.

Since *Leegin*, however, the ability of manufacturers to impose pricing restrictions on the resale of their products by distributors and retailers has been anything but clear, despite the Supreme Court's decision. Perhaps this should have been expected, given that in the *Leegin* case, more than 30 State Attorneys General urged the Supreme Court to continue to hold RPM agreements *per se* illegal. The Court's rejection of that position, therefore, raised an interesting question for the States: Would they follow federal antitrust precedent as to their state antitrust laws (as they typically do) on the RPM issue or reject the *Leegin* decision and continue to subject manufacturers to the potential for *per se* condemnation under their state antitrust laws.

The States Respond to *Leegin*

Over the course of the last five years, the answer has been "it depends," as the states have failed to take a uniform approach to the issue. Some State Attorneys General have staked out the position that RPM agreements remain *per se* unlawful under their particular state antitrust law and have brought enforcement actions predicated on that view. In California, for example, the State Attorney General has brought several enforcement actions in which the State maintained that *per se* treatment of RPM agreements remained the law under the Cartwright Act (California's antitrust law), notwithstanding *Leegin*. See *California v. Bioelements, Inc*., Cal. Super. Ct., Riverside Cty., No. 10011659 (Jan, 1, 2011); 100 Antitrust & Trade Reg. Rep. (BNA) 54 (Jan 21, 2011); *People v. Dermaquest*, Inc., Case No. RG 10497526 (Cal. Super. Ct. Alameda County, Feb. 23, 2010).

Similarly, in 2008, the Attorney General of New York, joined by the Attorneys General of Illinois and Michigan, brought an action against office furniture manufacturer Herman Miller, contending that its use of RPM agreements violated New York's antitrust law. *New York v. Herman Miller, Inc.*, 1:08-CV-2977-RMB (S.D.N.Y., March 21, 2008). The case was quickly settled by the defendant for $750,000, thus avoiding the opportunity for judicial resolution of whether, in fact, *per se* condemnation of RPM remained the law in New York post-*Leegin*. Notably, however, the New York courts subsequently addressed the issue in a different matter and rejected the view embraced by the New York Attorney General; instead, the court adopted the Supreme Court's holding in *Leegin* and ruled that RPM is *not per se* unlawful in New York. *Worldhomecenter.com v. Franke Consumer Prods.*, 2011 WL 2565284 (S.D.N.Y. 2011) (refusing to treat RPM as a *per se* violation of New York's Donnelly Act). That decision was also recently confirmed by another New York appellate court, *New York v. Tempur-Pedic International, Inc.*, 2012 N.Y. App. Div. LEXIS 3528 (May 8, 2012), in a second RPM enforcement action brought by the New York Attorney General. To date, however, the highest courts in neither California nor New York have addressed the issue, and thus the status of RPM in each of those states remains somewhat unsettled.

Another state struggling with the status of its RPM law is Tennessee. One federal district court has held that *Leegin's* "rule of reason" approach to RPM issues should be applied when interpreting Tennessee's antitrust law. See *Spahr v. Leegin Creative Leather Products*, 2008 WL 3914461 (E.D. Tenn. Aug 20, 2008) (applying Tennessee law). The ruling, while significant, is not a pronouncement from Tennessee's Supreme Court, and thus also leaves some room for uncertainty on the issue.

Finally, adding further confusion and uncertainty to the issue, legislation has been repeatedly introduced at the federal level, most recently by Senator Kohl (S. 75, 112 Cong., 21011-2012), that would overturn *Leegin* and again make RPM *per se* unlawful under the *federal* antitrust laws. While unlikely to pass this session, the possibility that federal law could change again with respect to RPM has made the decision regarding how to handle RPM issues all the more difficult for the states.

The *O'Brien* Decision

In the midst of this muddled scenario, the Kansas Supreme Court, in *O'Brien v. Leegin Creative Leather Products, Inc.*, No 101,000 (Kansas Sup. Ct. May 4, 2012), recently became the first state Supreme Court to issue a *definitive* ruling on the effect of *Leegin* on a state's RPM law. As explained in more detail below, the Kansas Supreme Court's holding - that *Leegin* has no bearing on how the Kansas state antitrust law should be interpreted and that RPM continues to be *per se* unlawful under Kansas law – is both clear and game-changing. First, however, a look at some of the specifics of the case.

By way of background, Leegin, the defendant in both the U.S. Supreme Court decision and the Kansas action, is a designer and manufacturer of fashion accessories and luggage, selling products throughout the United States through distributors and retailers. As the Kansas Supreme Court described, with respect to its Kansas operations, Leegin sold goods through retailers (as well as directly) and its retailers were required to agree to certain RPM restrictions as a condition of remaining a Leegin retailer. O'Brien, a consumer of Leegin products in Kansas, brought suit, contending that Leegin's RPM program constituted vertical price fixing that was *per se* illegal under Kansas state law. At the trial court level, the court, relying on *Leegin* and the Kansas courts' historical reliance on federal antitrust precedent when interpreting Kansas antitrust law, held that the rule of reason applied to Leegin's program, and that *per se* condemnation of the program was inappropriate. Under the rule of reason, the plaintiff failed to demonstrate antitrust injury arising from the Leegin RPM program (a necessary element of a rule of reason case), and thus plaintiff's claim failed.

The Kansas Supreme Court, however, disregarded both the U.S. Supreme Court's ruling in *Leegin* and the legal rationale underpinning it (the view that, in some circumstances, the institution of an RPM program can be either procompetitive or, at the very least, competitively-neutral), and instead held that the "rule of reason" does *not* apply to RPM lawsuits under the Kansas Restraint of Trade Act. Instead, such conduct continues to be *per se* unlawful in Kansas. In reaching this decision, Kansas joins Maryland as the only states that have *definitively* declared RPM *per se* unlawful under state law post-*Leegin*. (Maryland declared RPM *per se* unlawful through legislative action, not a court decision, passing legislation to that effect in 2009 – now codified at Md. Code. Ann., Comm. Law §11-204(b)).

Perhaps recognizing that the decision in *O'Brien* could impact the willingness of manufacturers to do business in the state (as has been rumored to have occurred in Maryland after the enactment of its legislation making RPM *per se* unlawful), less than a week after the Kansas Supreme Court's opinion was issued the Kansas legislature quickly entered the fray. HB 2797, a bill that would "correct the interpretation of the Kansas Restraint of Trade Act . . . made in *O'Brien v. Leegin Creative Leather Products, Inc.*" and "minimize conflicts between the Kansas Restraint of Trade Act and [federal law]" was introduced in the Kansas House. Reflecting a sense of urgency, the legislation provided that the new law would take effect immediately upon its publication in the Kansas register. The bill was quickly passed in the Kansas House on Saturday, May 16, by a wide margin. In the Senate, however, the bill (which had by then been repackaged and presented as an amendment to SB 416) came up for a vote on Sunday, May 17. While the bill received more votes in favor of passage than against, it failed to garner the statutorily required minimum number of votes required for passage and therefore was not adopted. Thereafter, the Kansas legislature promptly adjourned, leaving the *O'Brien* decision standing as the final word in Kansas on RPM issues.

The Aftermath

In light of *O'Brien*, and the failure of the proposed emergency legislation overturning it to be enacted by the Kansas legislature, no manufacturer doing business in Kansas can engage in RPM without facing significant potential legal exposure, risk that is much greater than that faced anywhere else in the country (other than Maryland). With this being the case, will national manufacturers seeking to implement national RPM programs decide that the legal risks in Kansas (and Maryland) make doing business in those states – at least through independent retailers – undesirable? In short, will corporate America's response to *O'Brien* be to declare, like Dorothy to Toto in the Wizard of Oz, that "We're not in Kansas anymore?" Only time will tell.

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