G. C. Thompson and G. P. Brady
Antitrust Fundamentals

Chapter 4

RESALE PRICE MAINTENANCE AND REFUSALS TO DEAL

VERTICAL PRICE FIXING AND FAIR TRADE

DR. MILES MEDICAL CO. v. JOHN D. PARK & SONS CO.[1]

Supreme Court of the United States, 1910.
220 U.S. 373, 31 S.Ct. 376, 55 L.Ed. 502.

MR. JUSTICE HUGHES, . . . delivered the opinion of the court.

The complainant, a manufacturer of proprietary medicines which are prepared in accordance with secret formulas, presents by its bill a system, carefully devised, by which it seeks to maintain certain prices fixed by it for all the sales of its products both at wholesale and retail. Its purpose is to establish minimum prices at which sales shall be made by its vendees and by all subsequent purchasers who traffic in its remedies. Its plan is thus to govern directly the entire trade in the medicines it manufactures, embracing interstate commerce as well as commerce within the States respectively. To accomplish this result it has adopted two forms of restrictive agreements limiting trade in the articles to those who become parties to one or the other. The one sort of contract known as "*Consignment Contract—Wholesale,*" has been made with over four hundred jobbers and wholesale dealers, and the other, described as *"Retail Agency Contract,"* with twenty-five thousand retail dealers in the United States.

The defendant is a wholesale drug concern which has refused to enter into the required contract, and is charged with procuring medicines for sale at "cut prices" by inducing those who have made the contracts to violate the restrictions. The complainant invokes the established doctrine that an actionable wrong is committed by one who maliciously interferes with a contract between two parties and induces one of them to break that contract to the injury of the other and that, in the absence of an adequate excuse . . .

The principal question is as to the validity of the restrictive agreements.

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The bill asserts complainant's "right to maintain and preserve the aforesaid system and method of contracts and sales adopted and established by it." It is, . . . a system of interlocking restrictions

1. Citations and footnotes omitted.

by which the complainant seeks to control . . . the prices for all sales by all dealers at wholesale or retail, whether purchasers or subpurchasers, and thus to fix the amount which the consumer shall pay, eliminating all competition. The essential features of such a system are thus described [by the Circuit Judge]: "The contracting wholesalers or jobbers covenant that they will sell to no one who does not come with complainant's license to buy, and that they will not sell below a minimum price dictated by complainant. Next, all competition between retailers is destroyed, for each such retailer can obtain his supply only by signing one of the uniform contracts prepared for retailers, whereby he covenants not to sell to anyone who proposes to sell again unless the buyer is authorized in writing by the complainant, and not to sell at less than a standard price named in the agreement. Thus all room for competition between retailers, who supply the public, is made impossible. If these contracts leave any room at any point of the line for the usual play of competition between the dealers in the product marketed by complainant, it is not discoverable. Thus a combination between the manufacturer, the wholesalers and the retailers to maintain prices and stifle competition has been brought about."

That these agreements restrain trade is obvious. That, having been made, as the bill alleges, with "most of the jobbers and wholesale druggists and a majority of the retail druggists of the country" and having for their purpose the control of the entire trade, they relate directly to interstate as well as intrastate trade, and operate to restrain trade or commerce among the several States, is also clear.

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The basis of the [complainant's] argument appears to be that, as the manufacturer may make and sell, or not, as he chooses, he may affix conditions as to the use of the article or as to the prices at which purchasers may dispose of it. The propriety of the restraint is sought to be derived from the liberty of the producer.

But because a manufacturer is not bound to make or sell, it does not follow that in case of sales actually made he may impose upon purchasers every sort of restriction. Thus a general restraint upon alienation is ordinarily invalid. "The right of alienation is one of the essential incidents of a right of general property in movables, and restraints upon alienation have been generally regarded as obnoxious to public policy, which is best subserved by great freedom of traffic in such things as pass from hand to hand. General restraint in the alienation of articles, things, chattels, except when a very special kind of property is involved, such as a slave or an heirloom, have been generally held void. 'If a man,' says Lord Coke, in Coke on Littleton, section 360, 'be possessed of a horse or any other chattel, real or personal, and give his whole interest or property therein, upon condition that the donee or vendee shall not alien the same, the same is void, because his whole interest and property is out of him, so as he hath no possibility of reverter; and it is against trade and traffic and bargaining and contracting between man and man.' " . . .

With respect to contracts in restraint of trade, the earlier doctrine of the common law has been substantially modified in adaptation to modern conditions. But the public interest is still the first consideration. To sustain the restraint, it must be found to be reasonable both with respect to the public and to the parties and that it is limited to what is fairly necessary, in the circumstances of the particular case, for the protection of the covenantee. Otherwise restraints of trade are void as against public policy. . . .

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The present case is not analogous to that of a sale of good will, or of an interest in a business, or of the grant of a right to use a process of manufacture. The complainant has not parted with any interest in its business or instrumentalities of production. It has conferred no right by virtue of which purchasers of its products may compete with it. It retains complete control over the business in which it is engaged, manufacturing what it pleases and fixing such prices for its own sales as it may desire. Nor are we dealing with a single transaction, conceivably unrelated to the public interest. The agreements are designed to maintain prices, after the complainant has parted with the title to the articles, and to prevent competition among those who trade in them.

The bill asserts the importance of a standard retail price and alleges generally that confusion and damage have resulted from sales at less than the prices fixed. But the advantage of established retail prices primarily concerns the dealers. The enlarged profits which would result from adherence to the established rates would go to them and not to the complainant. It is through the inability of the favored dealers to realize these profits, on account of the described competition, that the complainant works out its alleged injury. If there be an advantage to a manufacturer in the maintenance of fixed retail prices, the question remains whether it is one which he is entitled to secure by agreements restricting the freedom of trade on the part of dealers who own what they sell. As to this, the complainant can fare no better with its plan of identical contracts than could the dealers themselves if they formed a combination and endeavored to establish the same restrictions, and thus to achieve the same result, by agreement with each other. If the immediate advantage they would thus obtain would not be sufficient to sustain such a direct agreement, the asserted ulterior benefit to the complainant cannot be regarded as sufficient to support its system.

But agreements or combinations between dealers, having for their sole purpose the destruction of competition and the fixing of prices, are injurious to the public interest and void. They are not saved by the advantages which the participants expect to derive from the enhanced price to the consumer.

The complainant's plan falls within the principle which condemns contracts of this class. It, in effect, creates a combination for the prohibited purposes. No distinction can properly be made by reason of the particular character of the commodity in question. It is not entitled to special privilege or immunity. It is an article of commerce, and the rules concerning the freedom of trade must be held to apply to it. Nor does the fact that the margin of freedom is reduced by the control of production make the protection of what remains, in such a case, a negligible matter. And where commodities have passed into the channels of trade and are owned by dealers, the validity of agreements to prevent competition and to maintain prices is not to be determined by the circumstance whether they were produced by several manufacturers or by one, or whether they were previously owned by one or by many. The complainant having sold its product at prices satisfactory to itself, the public is entitled to whatever advantage may be derived from competition in the subsequent traffic.

The questions involved were carefully considered and the decisions reviewed [in the] opinion of the Circuit Court of Appeals. [I]t was concluded below that the restrictions sought to be enforced by the bill were invalid both at common law and under the act of Congress of July 2, 1890. We think that the court was right.

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Judgment affirmed.

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1. Note that *Dr. Miles* came just before the formulation of the rule of reason in the 1911 *Standard Oil* case. The *Dr. Miles* holding has since been reaffirmed on several occasions. Is its rationale still sound? If not, can a substitute rationale be formulated?

2. Suppose a group of dealers are practicing price leadership in a lawful way. The manufacturer of a popular article wants to encourage volume distribution at a lower price. To achieve this result, the manufacturer offers reduced prices at the wholesale level to any retailers who will lower prices at the retail level by at least a specific sum. Has the manufacturer engaged in unlawful price fixing?

THE MOVEMENT TO FAIR TRADE

Many sellers attempted to justify resale price maintenance as the only means to protect their good will and preserve the integrity of their trade names. Without these agreements, they argued, they were at the mercy of cut-throat price wars among the retailers. The

Supreme Court consistently rejected this attempted justification. At the same time, small retailers argued that price wars threatened their survival, and that fixed retail prices would preserve them as competitors with chain and department stores. During and after the 1930's, many states validated resale price agreements by means of statutes known somewhat euphemistically as "fair-trade" laws. These statutes authorized suppliers of trademarked or branded products to require retailers not to sell the goods below a specified minimum price. At first these fair-trade statutes applied only to those retailers who had actually signed the minimum price agreements. Such arrangements were impotent because "nonsigners," often constituting the bulk of competitors on the distributing level, were still free to cut prices. Later state statutes closed this loophole by providing that *all* distributors, including nonsigners, were bound once they knew that a fair-trade agreement had been signed by *any* distributor. In 1936 the constitutionality of the statutes was upheld in Old Dearborn Distrib. Co. v. Seagram Distillers Corp., 299 U.S. 183 (1936), as a valid exercise of state police power.

Some resale price maintenance agreements were exempted from antitrust restrictions by the Miller Tydings Act of 1937 and the McGuire Act of 1952. The exemption was eliminated by the Consumer Goods Pricing Act of 1975.

REFUSALS TO DEAL TO ENFORCE RESALE PRICE MAINTENANCE

One method to achieve resale price maintenance, without recourse to fair-trade legislation, is to refuse to deal. To maintain a given retail price, a manufacturer announces that its policy is to refuse to sell to any retailers quoting a lower price, and thereafter the manufacturer ceases selling to any price-cutting retailers. This circumvention of *Dr. Miles* was approved in United States v. Colgate & Co., 250 U.S. 300 (1919), where the court affirmed:

> In the absence of any purpose to create or maintain a monopoly, the act does not restrict the long recognized right of trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal; and, of course, he may announce in advance the circumstances under which he will refuse to sell.