Antitrust Law: A Long Time Coming—United States Supreme Court Adopts the "Rule of Reason" Test for Vertical Maximum Price Fixing Cases in State Oil Co. v. Khan

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NOTES

Antitrust Law: A Long Time Coming — United States Supreme Court Adopts the "Rule of Reason" Test for Vertical Maximum Price Fixing Cases in State Oil Co. v. Khan

I. Introduction

Any astute observer of the retail gasoline industry in Oklahoma over the last thirty years can attest to the proliferation of brand name retail gasoline service stations. It seems as though there is a nice, clean Texaco, Conoco, or Phillips 66 service station on almost every corner. However, with the rise of the so-called brand name gas stations, one can also observe the decreased number of independent retailers of gasoline. The small independent seller has been pushed aside as more oil and gas companies have vertically integrated their businesses to handle the exploration, production, refining, and marketing of gasoline. The average Oklahoman may be unaware that the incentives for oil companies and other major corporations to engage in vertical integration were created in part by the United States Supreme Court's decision in Albrecht v. Herald Co., an antitrust case decided over thirty years ago.

In Albrecht, the Court held that vertical maximum price fixing was per se illegal; however, thirty years after this decision, the Supreme Court finally recognized the error of its decision. In 1997, in State Oil Co. v. Khan, the Supreme Court overruled Albrecht, and vertical maximum price fixing is now judged under a rule of reason analysis. The decision in Khan may have come too late for many independent Oklahoma gas station retailers adversely affected by the previous decision in Albrecht. However, the economic reasoning employed by the Court in Khan signals a major victory for consumers in Oklahoma and around the nation. In order to understand the ramifications of the Khan decision, it is necessary to examine the historical evolution of antitrust law with regard to vertical restraints of trade and the development of the two main evidentiary tests in this area, the per se rule and the rule of reason.

In 1890, Congress passed the Sherman Antitrust Act. The purpose of the Sherman Act was to promote competition and increase consumer welfare. Section

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2. See id. at 152.
4. See id.
5. Scholars disagree concerning Congress' ultimate goals in passing the Sherman Act. See Robert H. Lande, Wealth Transfers as the Original and Primary Concern of Anti-trust: The Efficiency
1 of the Act contains two main parts. First, two independent entities must "agree" to violate the Act. Second, the agreement must unreasonably restrain trade.6

For more than one hundred years, the judiciary has interpreted the meaning of section 1 of the Sherman Act. The judiciary's task has been difficult due to the brevity and the ambiguity of the language in this provision. The courts have recognized that section 1 does not mean literally what it says.7 If read literally, all contracts would violate the Sherman Act because all contracts restrain trade to a certain degree. Clearly, this type of interpretation would grind the wheels of commerce to a complete halt. Thus, the judiciary had to develop certain rules and techniques which define illegal conduct under the Act.

Section 1 violations arise in both a horizontal and vertical context. Horizontal restraints of trade involve agreements among competitors at the same level in an industry to restrain trade through price fixing.8 In contrast, vertical restraints of trade involve agreements between firms at different levels in an industry, such as a manufacturer and a wholesaler or a wholesaler and a retailer, to do one of several things.9 First, vertical agreements may set either a minimum or maximum price at which the product will ultimately be distributed to the customer. This type of conduct is generally termed resale price maintenance (RPM). Vertical agreements may limit distributors to an exclusive territory, or vertical agreements might require retailers to deal only in the products of a certain manufacturer. This type of agreement is commonly referred to as an exclusive dealing arrangement.

Interpretation Challenged, 34 HASTINGS L.J. 67, 68 (1982) ("The prevailing view is that Congress intended the antitrust laws only to increase economic efficiency. Others, however, contend that Congress was largely motivated by a number of social, moral, and political concerns."). This disagreement arises for two primary reasons. First, the language of the Sherman Act is ambiguous. Second, the legislative history of the Sherman Act contains conflicting statements. See id. at 81. However, modern antitrust theory regards the maximization of consumer welfare as one of the most important values in modern antitrust analysis. For a more detailed discussion of the importance of consumer welfare in modern antitrust analysis, see Robert H. Bork, Legislative Intent and the Policy of the Sherman Act, 9 J.L. & ECON. 7 (1966) (concluding, based upon evidence in the Congressional Record, that Congress intended the courts to take into account in the decision of cases only that value known as consumer welfare).

6. See 15 U.S.C. § 1 (1994) ("Every contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce among the several States, or with foreign nations is hereby declared to be illegal.").

7. See id. The Supreme Court has recognized that section 1 does not prohibit "every" agreement in restraint of trade. Instead, only those agreements which unreasonably restrain trade violate section 1 of the Act. See Brooking v. International Motor Contest Ass'n, No. CIV. C96-134MJM, 1998 WL 937242, at *1 (N.D. Iowa 1998) (citing Northern Secs. Co. v. United States, 193 U.S. 197 (1904); United States v. Joint-Traffic Ass'n, 171 U.S. 505 (1898)). As Justice Holmes eloquently stated in Northern Securities, an interpretation that "every" agreement in restraint of trade violates section 1 would have "made eternal the bellum omnium contra omnes and disintegrated society so far as it could into individual atoms." Northern Secs. Co., 193 U.S. at 411.

8. Horizontal restraints of trade are usually deemed more anti-competitive and hence worse than vertical restraints. A horizontal restraint of trade is an agreement among competitors at the same level in the industry to restrain trade through price fixing. Horizontal restraints of trade are not the focus of this article and are treated differently by the courts.

Finally, vertical agreements could require customers to take additional products if they want to purchase a particular product from the manufacturer. The final example is called a tying arrangement.  

Since the early part of the twentieth century, the Supreme Court has vacillated in its treatment of vertical restraints of trade under section 1 of the Sherman Act. The Court at different times has applied two evidentiary tests to interpret vertical restraint cases brought under section 1 of the Sherman Act. The two tests are the per se rule and the rule of reason test.

Some combinations in restraint of trade are judged under the per se rule. Agreements which fall under the per se rule are deemed to be inherently illegal. The standard for determining when the per se rule applies to vertical restraint of trade cases is best articulated in *Northern Pacific Railway Co. v. United States.* In that case, the Court stated that "agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable, and therefore, illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use."  

In contrast, the rule of reason test is a less stringent means of analyzing whether a violation of section 1 of the Sherman Act has occurred. The rule of reason test requires the judge and jury to analyze the nature of the restraint, the market structure of the industry in question, and other economic factors in determining whether the combination violates section 1 of the Sherman Act. Perhaps the rule was stated best by Justice Brandeis in *Chicago Board of Trade v. United States.* The Court found that "the true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition."  

It is clear that a court's decision as to which of the aforementioned tests to apply is critical to an efficient system of justice in the area of vertical restraints. The per se rule has several benefits. First, the per se rule promotes judicial economy. A court employing the per se rule does not have to undergo a full-blown economic analysis to determine if there are sufficient pro-competitive justifications for permitting the conduct in each individual case. Second, the per se rule gives the business community a clear standard for determining whether conduct is illegal. Third, the per se rule allows plaintiffs to have a reasonable opportunity to win cases which would not even be filed if the rule of reason were the governing test.

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10. *See id.*  
12. *Id.* at 5.  
15. *Id.* at 238.  
17. *See id.*  
18. *See id.*
Conversely, the rule of reason is a balancing test that could be described as more detailed in a certain sense than the per se rule. With the rule of reason, a court determines if the pro-competitive effects of the conduct outweigh the anti-competitive effects. If so, the conduct is deemed legal.\textsuperscript{19} The rule of reason test, then, is most appropriate in situations where it is unclear whether the activity has a severe, detrimental effect on competition.

The utilization of one test over the other also has great practical importance for litigants in a vertical maximum price fixing case. The plaintiff will often prevail if given a per se jury instruction. In contrast, the defendant will almost always win if the court employs a rule of reason analysis. As such, the test employed will more than likely determine the outcome of a particular case.\textsuperscript{20}

This note will examine the reasons for the change from a per se test to a rule of reason analysis in vertical maximum price fixing cases. First, this note will point out that the per se rule in vertical maximum price fixing cases was a product of historical precedent, rather than detailed economic analysis. Second, this note will demonstrate why the Albrecht decision violated the purposes of the Sherman Act. Third, the note will explain why Khan appropriately changed the law in this area. Finally, in light of the recent passage of the Oklahoma Antitrust Statute, the note will evaluate the impact of the rule of reason test in vertical maximum price fixing cases in Oklahoma.

\textbf{II. Background/History}

The seminal case in the area of vertical restraints was a 1911 Supreme Court case, \textit{Dr. Miles Medical Co. v. John D. Park & Sons Co.}\textsuperscript{21} In \textit{Dr. Miles}, the Supreme Court determined that producer contracts with jobbers, wholesale druggists, and retailers, which ultimately fixed retail prices on proprietary medicine, violated section 1 of the Sherman Act.\textsuperscript{22}

The Dr. Miles Medical Co. was a large manufacturer of proprietary medicines, which had used its power in the industry to negotiate two types of contracts: a "Consignment Contract — Wholesale" and a "Retail Agency Contract."\textsuperscript{23} The "Consignment Contract — Wholesale" involved four hundred jobbers and wholesale dealers.\textsuperscript{24} The "Retail Agency Contract" involved twenty-five thousand retail dealers in the United States.\textsuperscript{25} The purpose of the contracts was to fix a minimum price beneath which all sales of the medicines at both the wholesale and retail level would not fall.\textsuperscript{26}

\textsuperscript{19} See United States v. Addyston Pipe & Steel Co., 175 U.S. 211 (1899).
\textsuperscript{20} See Pitofsky, supra note 16, at 1489-90.
\textsuperscript{21} 220 U.S. 373 (1911).
\textsuperscript{22} See id. at 409.
\textsuperscript{23} See id. at 375, 379.
\textsuperscript{24} See id. at 383.
\textsuperscript{25} See id.
\textsuperscript{26} See id. at 378.
The *Dr. Miles* Court reasoned that the vertical minimum price fixing controls employed by the producer of the medicines stifled competition among wholesalers and retailers. The Court deemed these types of vertical agreements to be injurious to the public interest. Once the producer has sold the product at prices satisfactory to itself, the public (consumers) is entitled to whatever advantage may be derived from competition in the subsequent traffic.

In a vigorous dissent, Justice Holmes attacked the majority reasoning. Justice Holmes questioned the logic of interfering with business activity agreed to by each of the parties in the production-distribution chain simply because the price charged to the public was not a "fair" price. In a key part of his dissent, Justice Holmes stated:

> I think that we greatly exaggerate the value and importance to the public of competition in the production or distribution of an article (here it is only distribution) as fixing a fair price. What really fixes that is the competition of conflicting desires. We, none of us, can have as much as we want of all the things that we want. Therefore, we have to choose. As soon as the price of something that we want goes above the point at which we are willing to give up other things to have that, we cease to buy it and buy something else.

As interpreted by later Supreme Court decisions, *Dr. Miles* stood for the proposition that vertical minimum price fixing is per se illegal. The *Dr. Miles* decision is important because it influenced the development of the per se test in vertical maximum price fixing cases. Unfortunately, later courts failed to distinguish between vertical minimum price fixing, which would ultimately harm the consumer by reducing competition, and vertical maximum price fixing, which actually benefits the consumer by ensuring that the price of a product will not be raised above a certain level.

In order for a plaintiff to win a vertical maximum price fixing case, the plaintiff must establish that an agreement existed to fix prices at a certain level. In 1919, the Supreme Court decided *United States v. Colgate*, which clarified the agreement element for all types of vertical price fixing cases. The *Colgate* Court drew a distinction between a dealer's contractual obligation to resell at fixed prices, such as the situation in *Dr. Miles*, and an independent dealer's decision to price his product as he wishes.

27. See id. at 400.
28. See id. at 408.
29. See id.
30. See id. at 409.
31. See id. at 412.
32. Id.
33. 250 U.S. 300 (1919).
34. See id. at 306.
In Colgate, the evidence indicated that the manufacturer had sent lists of prices to the dealer recommending prices for resale.\textsuperscript{35} Furthermore, it was alleged that no further sales would be made to those dealers who did not adhere to the "recommended" resale price.\textsuperscript{36}

The Court reasoned as follows:

In the absence of any purpose to create or maintain a monopoly, the act does not restrict the long recognized right of a 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.\textsuperscript{37}

The Colgate decision makes it more difficult for a plaintiff to win a vertical maximum resale price maintenance case. If there is no "agreement" on price levels, then the plaintiff will not be able to prevail, even if the restraint is per se illegal. The Colgate decision is critical because it limits the instances in which the per se rule against vertical maximum resale price maintenance applies.

The Dr. Miles holding and the Colgate doctrine set the stage for the development of the law of vertical maximum price fixing. The next section will further illustrate why vertical maximum price fixing was per se illegal until 1997.

### III. Law Prior to the Case

The origins of the per se rule as applied to vertical resale price maintenance agreements can be traced back to the Supreme Court's decision in United States v. Socony-Vacuum Oil Co.\textsuperscript{38} In Socony-Vacuum, the Court held that a horizontal agreement among competitors which has the effect of either raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal per se under the Sherman Act.\textsuperscript{39} The Court went a step further in contradicting the notion that economic justifications for price fixing should play a part in the legal analysis. According to the Court, any combination which meddles with price structures is engaged in an unlawful activity. It is immaterial whether the price-fixers are in an economic position to control the market. Price fixing agreements which raise, lower, or stabilize prices are unlawful because they disrupt the free play of market forces.\textsuperscript{40}

The Socony-Vacuum analysis appeared to indicate that maximum vertical price fixing agreements should be deemed per se illegal. After all, this type of

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\textsuperscript{35} See id. at 303.
\textsuperscript{36} See id.
\textsuperscript{37} Id. at 307.
\textsuperscript{38} 310 U.S. 150 (1940).
\textsuperscript{39} Id. at 223.
\textsuperscript{40} See id. at 221.
agreement has the effect of "stabilizing" the price. Indeed, the court adhered to this
logic in Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.\textsuperscript{41}

In Kiefer-Stewart, two distillers mandated a maximum resale price to their
distributors above which the distributor could not charge.\textsuperscript{42} The Court determined
that the fixing of a horizontal maximum resale price violates the Sherman Act.\textsuperscript{43}
The Court reasoned that horizontal maximum resale price fixing is as pernicious as horizontal minimum price fixing because both types of conduct limit the
freedom of traders to sell in accordance with their own judgment of the
marketplace.\textsuperscript{44}

Of course, neither Socony-Vacuum nor Kiefer-Stewart required the Court to
address the issue of vertical maximum price fixing. However, the rationale
outlined in Socony-Vacuum and Kiefer-Stewart foreshadowed the formalistic line-
drawing of the Albrecht Court in the area of vertical maximum restraints. In both
Socony-Vacuum and Kiefer-Stewart, the Court stipulated that the free play of
market forces, along with the freedom of traders to exercise their own judgment,
were the most important values to be protected by the Sherman Act.\textsuperscript{45} The
Albrecht holding that vertical maximum price fixing is per se illegal reinforced the
importance of these values.\textsuperscript{46} Fortunately, Khan shifted the focus of the inquiry
in vertical maximum price restraint cases toward the issue of whether the agreement to fix prices adversely affects the consumer and competition in the
marketplace. The ultimate goal of the Sherman Act remains to protect competition
and not individual competitors.

Vertical maximum price fixing cases implicitly suggest that the consumer is
actually helped by these agreements. A contractual ceiling, above which the
wholesaler or retailer is unable to charge, is placed on the price. The retailer can
choose to price lower than the ceiling, but prices cannot rise above the ceiling
price. Thus, the consumer will ultimately pay lower prices. Based on the
fundamental idea of the Sherman Act as a "consumer welfare" prescription, why
would the law want to outlaw this type of activity? Indeed, there does not seem
to be an appropriate consumer-based economic reason to condemn these types of
agreements. That is why the Albrecht holding was so shocking.

In Albrecht, the Supreme Court held that vertical maximum price fixing is per
se illegal because maximum prices substitute the perhaps erroneous judgment of
a seller for the forces of the competitive market.\textsuperscript{47} Yet, the Court employed no
economic analysis to demonstrate how fixing a maximum price would harm
competition, and ultimately the consumer. Consequently, the Albrecht decision
ignored economic reality and violated the fundamental purposes of the Sherman
Act.

\textsuperscript{41} 340 U.S. 211 (1951).
\textsuperscript{42} See id. at 212.
\textsuperscript{43} See id. at 213.
\textsuperscript{44} See id.
\textsuperscript{45} See Socony-Vacuum, 310 U.S. at 221; Kiefer-Stewart, 340 U.S. at 213.
\textsuperscript{47} See id. at 152.
Albrecht involved a morning newspaper which distributed its paper through the use of independent carriers. The independent carriers bought the paper at wholesale prices and sold them to consumers at retail prices. The independent carriers were given exclusive territories (routes) in which to sell the paper. The newspaper communicated a maximum resale price for the paper to each carrier. The agreement clearly stated that a carrier's right to distribute the product would be terminated if the carrier sold above the resale price. However, one of the carriers raised the retail price above the maximum set by the newspaper. The newspaper, after failing to convince the carrier to rectify the retail price, terminated the carrier's right to distribute the paper. The carrier was forced to sell the route to a replacement carrier which adhered to the newspaper's recommended maximum price.

Albrecht elucidates that it is often in the manufacturer's economic self-interest to engage in vertical maximum price fixing. An exclusive territory for a carrier gives the carrier a natural monopoly. This monopoly allows the carrier to raise the price of the newspaper above the maximum. The carrier can maximize its profits by reducing output below the competitive level. The entire monopoly profit generated by this pricing, however, will be pocketed by the carrier and not the newspaper. In fact, the newspaper is adversely affected by the monopoly price in two ways. First, it loses money from the reduced circulation. Second, it suffers a further blow because the decreased circulation leads to decreased advertising revenue.

The consequences of the carrier's action also adversely affect the consumer. Instead of paying a competitive price for his newspaper, the consumer gives back a portion of his consumer surplus by having to pay the monopoly price. From this basic economic perspective, the newspaper's maximum resale price actually works to set a competitive price, which in the absence of newspaper action would probably result in a monopolist price. Thus, the establishment of the maximum resale price benefits both the newspaper and the consumer.

Despite the benefits of this type of agreement to the consumer, the Albrecht Court proposed three reasons why vertical maximum price fixing should be declared per se illegal. First, the Court opined that maximum prices may be fixed too low for the dealer to furnish essential services to the consumer. Second, the

48. See id. at 147.
49. See id.
50. See id.
51. See id.
52. See id.
53. See id. at 148.
54. See id.
55. SULLIVAN & HOVENKAMP, supra note 9, at 426.
56. See id.
57. See id.
58. See id.
59. See id.
Albrecht rationale stated that maximum price fixing may channel distribution through a few large or specifically advantaged dealers who otherwise would be subject to significant non-price competition.\textsuperscript{61} Third, the Court reasoned that vertical maximum price fixing by suppliers could interfere with dealer freedom.\textsuperscript{62} However, as will be discussed later, none of these justifications for the imposition of the per se rule are particularly persuasive.

The Albrecht decision has been widely criticized by legal scholars for its failure to apply rigorous economic analysis to support its conclusions.\textsuperscript{63} Almost all lower federal courts realized the inherent problems with the application of the per se rule in this context. As such, the courts attempted to limit the harshness of the rule when possible. Knutson \textit{v. Daily Review, Inc.}\textsuperscript{64} and Northwest Publications, \textit{Inc. v. Crumb}\textsuperscript{65} illustrate how courts attempted to alleviate the negative effects of the per se rule. Both Knutson and Northwest Publications involved substantially the same facts as Albrecht. The defendants were newspaper publishers who inserted maximum price maintenance clauses in their contracts with independent distributors for all the reasons previously mentioned.\textsuperscript{66} In Northwest Publications, the Ninth Circuit held that the maximum price fixing clause was a per se violation but determined that the plaintiff-distributors were not entitled to damages because of a failure to prove a causal relationship between the illegal price fixing and a loss of profits.\textsuperscript{67}

The Northwest Publications court reasoned that competitive forces would have caused the distributors to maintain the same long-range price as the one the publisher had chosen as the maximum.\textsuperscript{68} The court relied on evidence that the distributors had not raised their price above the maximum until one year after they learned the price fixing clause was illegal.\textsuperscript{69} The court surmised that the distributors knew that a failure to maintain a price below the maximum established by contract would cause the publisher to terminate them and to vertically integrate their operations.\textsuperscript{70} The distributor's fear of termination explained the one year delay in raising the price above the maximum. The court reasoned that a short-term termination clause is a competitive market force, and that the threat of vertical integration by the publisher would have caused the distributors to maintain the same price absent an agreement. Therefore, the distributors suffered no damages.\textsuperscript{71}

\begin{footnotes}

\footnotetext[61]{See id. at 153.}
\footnotetext[62]{See id.}
\footnotetext[63]{See, e.g., Frank Easterbrook, \textit{Maximum Price Fixing}, 48 U. Chi. L. REV. 886, 889 (1981).}
\footnotetext[64]{468 F. Supp. 226 (N.D. Cal. 1979).}
\footnotetext[65]{752 F.2d 473 (9th Cir. 1985).}
\footnotetext[66]{See Herbert Hovenkamp, \textit{Vertical Integration by the Newspaper Monopolist}, 69 IOWA L. REV. 451, 452-56 (1984).}
\footnotetext[67]{See Northwest Publications, 752 F.2d at 475, 477.}
\footnotetext[68]{See id. at 477.}
\footnotetext[69]{See id. at 476.}
\footnotetext[70]{See id.}
\footnotetext[71]{See id. at 477.}
\end{footnotes}
The Knutson court employed similar reasoning. The court outlined the following test for determining whether a plaintiff is entitled to antitrust damages from an illegal vertical maximum price fixing agreement. The court stated that the plaintiff-distributor must present evidence that the profit maximizing price was higher than the fixed price.\(^{72}\) If the evidence presented supports this contention, plaintiffs are entitled to a rebuttable presumption that the distributors would have charged that higher price to their customers.\(^{73}\)

In applying this test, the Knutson court relied on the "time lag" and "vertical integration" evidence established by the publisher to determine that the presumption had been rebutted.\(^{74}\) The court noted that a significant time lag existed between the date of price freedom and any raising of prices above the maximum.\(^{75}\) The court also relied on testimony by the publisher that the distributor knew any movement in price above the maximum set by the publisher would result in the publisher converting to an employee distribution system.\(^{76}\) Thus, the court concluded that no causation existed between the illegal price fix and any loss of profits.\(^{77}\)

Undoubtedly, the "causation" requirements imposed by the Knutson and Northwest Publications courts helped alleviate the poor decision in Albrecht. However, not all courts were as creative in attempting to circumvent the harsh effects of the per se rule. In Shafer v. Bulk Petroleum Corp.,\(^{78}\) the United States District Court for the Eastern District of Wisconsin denied a defendant's motion for summary judgment in a maximum resale price maintenance case.\(^{79}\) The court held that it was per se illegal for a large oil company to institute a vertical maximum price fixing agreement with independent retailers of gasoline.\(^{80}\)

In Shafer, the defendant was a wholly owned subsidiary of Gulf Oil Corporation, a large refiner and supplier of petroleum products in the United States.\(^{81}\) The plaintiffs operated discount unbranded gasoline retail outlets.\(^{82}\) The defendants sold gasoline to the plaintiffs but set a maximum price above which the plaintiffs could not price their product.\(^{83}\) The court determined that a per se standard applied because Albrecht made vertical maximum price fixing per se illegal.\(^{84}\)

Knutson, Northwest Publications, and Shafer illustrate the perverse incentives created by the Albrecht decision. The Albrecht decision encouraged manufacturers to discontinue business relationships with independent retailers. Manufacturers are

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73. See id. at 235.
74. See id. at 236-37.
75. See id.
76. See id. at 237.
77. See id. at 240.
78. 569 F. Supp. 621 (E.D. Wis. 1983).
79. See id. at 630.
80. See id. at 625.
81. See id. at 623.
82. See id.
83. See id. at 622.
84. See id. at 624-25.
discouraged from maintaining business relationships with independent retailers if maximum resale pricing programs, enacted to ensure that a product is priced at a competitive level, violate the antitrust laws. Instead, if a maximum resale price agreement creates antitrust exposure, a manufacturer may decide it is economically more efficient to vertically integrate operations.

As it turns out, not only was Albrecht anti-consumer, it was also anti-independent retailer and pro-vertical integration. It is likely that executives at Gulf Oil Corporation, after learning of the per se standard as outlined in Shafer, would question spending millions of dollars on legal fees to defend their practice of instituting maximum resale price maintenance agreements. Instead of persisting through all of the legal hassles, why not simply vertically integrate? At least in Oklahoma, many large oil companies indeed decided vertical integration to be the appropriate business strategy.85

The next major practical limitation of the per se rule in vertical maximum price fixing cases came in Atlantic Richfield Co. v. USA Petroleum Co.86 The Atlantic Richfield Court further clarified the requirements of antitrust injury. The Court held that competitors of dealers burdened by a supplier's unlawful maximum vertical price fix do not suffer antitrust injury and thus are not beneficiaries of the per se rule outlined in Albrecht.87 Unfortunately, the Court failed to use this opportunity to address the applicability of the per se rule to vertical maximum price fixing. The Court, however, did imply that Albrecht may not have been correctly decided.88 It was not until State Oil Co. v. Khan that the Court finally directly confronted its ill-fated decision thirty years past.

IV. Statement of the Case

A. Facts

In Khan, an individual retailer, Barkat Khan, signed an exclusive requirements contract with State Oil Company in 1992 for the lease and operation of a Unocal 76 service station and convenience store near Chicago.89 The contract required

85. See Clytie Banyan, Oklahoma City Nears Top of Nation in Minimarts Per Capita, Survey Says, Daily Oklahoman, Apr. 4, 1999, at 1-C, 3-C. A 1998 survey by MPSI Systems, Inc., a Tulsa-based international marketing research company, indicated that Oklahoma City has among the highest number of convenience stores per capita in the United States. See id. Convenience stores sell both gasoline and groceries. See id. Four of the six market leaders in retailing gas and groceries are major oil companies. See id. They include Conoco, Phillips Petroleum Co., Texaco, and Total Petroleum Co. Furthermore, of the 3300 convenience stores in Oklahoma, the Conoco label is affixed to 400 stores, and the Phillips Petroleum label is affixed to 430 statewide locations. See id. However, these figures include stores owned by the oil companies and stores which the oil companies allow independent marketers to use their name. See id.
87. See id. at 339.
88. See id. at 328, 335 n.5 ("We assume arguendo that Albrecht correctly held that vertical, maximum price fixing is subject to the per se rule.").
89. See State Oil Co. v. Khan, 118 S. Ct. 275, 278 (1997).
Khan to purchase fuel and other products solely from State Oil. 90 State Oil sold various grades of gasoline to Khan at 3.25 cents less per gallon than States Oil's suggested resale price for each grade. 91 If Khan chose to raise his selling price on fuel above the State Oil suggested resale price, Khan had to remit any difference above the 3.25 cent margin to State Oil. 92 Thus, Khan had the freedom to charge as high a price as he wished without breaching his contract with State Oil. Nevertheless, since all the profits derived by Khan from pricing above State Oil's suggested retail price would accrue to State Oil, obviously it was fruitless for Khan to raise his price above the suggested maximum. Consequently, the State Oil contract was a vertical maximum price fixing agreement. 93

Within the first year of the contract, State Oil evicted Khan from the property for failing to make rent payments and terminated the contract. 94 After the termination, Khan brought suit in the United States District Court for the Northern District of Illinois alleging State Oil had engaged in vertical maximum price fixing in violation of section 1 of the Sherman Act. 95

B. Issue

The Supreme Court agreed with the Seventh Circuit Court of Appeals that the contractual provision in question operated as a vertical maximum price fixing agreement. 96 Thus, the main issue for the Supreme Court was whether the vertical maximum price fixing agreement was subject to the per se rule. If the agreement was per se illegal, State Oil violated section 1 of the Sherman Act. 97 On the other hand, if the vertical maximum price fixing agreement was governed by the rule of reason, State Oil could argue that this particular agreement promoted rather than hindered competition.

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90. See id.
91. See id.
92. See id. at 8.
93. See Khan v. State Oil Co., 93 F.3d 1358, 1360-61 (7th Cir. 1996). Noted antitrust scholar and current Seventh Circuit Federal Judge Richard Posner authored the opinion at the circuit level. Judge Posner entertained the argument that the contractual provision in question was not a price fix because Khan would not breach the contract by raising the price above State Oil's suggested maximum price. State Oil argued that it was not a true price fix because State Oil did not threaten to terminate Khan's lease if he priced above the maximum suggested retail price. See id. However, Judge Posner dismissed this argument as a distinction without a difference for purposes of determining whether vertical maximum price fixing occurred. See id. Judge Posner stated, "There is no practical difference between that form of words (threat to terminate the lease) and permitting Khan to sell at a higher price but providing that if he does so the profit belongs to State Oil." Id. Consequently, the court found State Oil engaged in vertical maximum price fixing. See id.
94. See Khan, 118 S. Ct. at 278.
95. See id.
96. See id. at 279.
97. Recall that the application of the per se rule makes it unnecessary for the trier of fact to analyze the economic effects of the agreement in question. See Northern Pac. Ry. Co. v. United States, 356 U.S. 1, 5 (1958).
C. Procedural History/Holding

The Seventh Circuit reversed the district court's grant of summary judgment to State Oil. Writing for the majority, Judge Posner noted the pro-competitive justifications for this type of vertical restraint, but determined that the district court's decision to employ a rule of reason analysis was inappropriate.\(^9\) Judge Posner concluded that the Albrecht decision governed the dispute before the court.\(^9\) Under Albrecht, all vertical maximum price fixing agreements were per se illegal. Because Khan could not fairly be distinguished from Albrecht, stare decisis mandated a finding that the vertical maximum price fixing agreement at issue was per se illegal.\(^10\) However, the Supreme Court vacated the judgment of the Seventh Circuit Court of Appeals. In a unanimous opinion, the Supreme Court overruled Albrecht. The Court held that all vertical maximum price fixing agreements should be judged under a rule of reason analysis.\(^10\)

D. Reasoning

As mentioned previously, Albrecht proposed three reasons why vertical maximum price-fixing cases were to be governed by the per se test. The Khan court criticized each of these reasons as insufficient for the continued adherence to the per se standard.\(^10\)

First, the Albrecht Court opined that maximum prices may be fixed too low for the dealer to furnish essential services to the consumer.\(^10\) The Khan Court, however, reasoned that a supplier is unlikely to set such a price as a matter of business judgment because such conduct would ultimately decrease the number of purchasers and thereby decrease the supplier's profits.\(^10\) Second, the Albrecht rationale stated that maximum price-fixing may channel distribution through a few large or specifically advantaged dealers who otherwise would be subject to significant non-price competition.\(^10\) However, the Khan Court pointed out that it is unclear how a supplier would profit from limiting its market by excluding potential dealers.\(^10\) Moreover, although the allowance of vertical maximum price fixing might harm smaller, inefficient dealers, it would not harm competition and consumer welfare.\(^10\) Third, the Albrecht rationale stated that vertical maximum price-fixing by suppliers could interfere with dealer freedom.\(^10\) However, the Khan Court noted certain studies which indicated the Albrecht decision simply

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98. See Khan, 93 F.3d at 1362.
99. See id.
100. See Khan, 118 S. Ct. at 279.
101. See id. at 285.
102. See id. at 282-83.
103. See id. at 282.
104. See id.
105. See id. at 283.
106. See id.
107. See id.
108. See id.
provided incentives for suppliers to integrate forward into distribution, thereby destroying the so-called dealer freedom because the dealer does not exist. 109

Despite the problematic nature of Albrecht, Khan argued that per se illegality for vertical maximum price-fixing agreements should be maintained. 110 Khan argued that the principle of stare decisis mandated continued adherence to the per se rule. 111 However, Khan failed to persuade the Court that stare decisis should be utilized to reinvigorate a decision whose foundation had been utterly destroyed by antitrust scholars, practitioners, and judges. 112

Khan cited Toolson v. New York Yankees, Inc. 113 and Flood v. Kuhn 114 for the proposition that the principle of stare decisis combined with the failure of the Congress to pass legislation which would overrule an interpretation by the Supreme Court mandates adherence to the per se rule. 115 The Supreme Court rejected this proposition for two reasons. First, the Court determined that Toolson and Flood are anomalies because these cases concern Major League Baseball. General antitrust principles do not apply to this industry. 116 Second, stare decisis is not an inexorable command. The Court reasoned that considerable deference should be given to the judiciary to overrule antitrust precedent because this area of the law is particularly influenced by the lessons of economic experience as well as current economic theory. 117

V. Analysis

A. Practical Implications of State Oil v. Khan

The Supreme Court correctly changed the evidentiary standard in vertical maximum price fixing cases from a per se test to a rule of reason analysis. The application of the rule of reason test does not mean that all vertical maximum price fixing agreements will be legal. However, in the aftermath of Khan, private plaintiffs will find it extremely difficult to prevail on an allegation that a manufacturer in a vertical relationship with a supplier or retailer illegally fixed a maximum resale price. Khan implies that most vertical maximum price agreements will pass the rule of reason test, absent extraordinary circumstances.

110. See Khan, 118 S. Ct. at 283-84.
111. See id.
112. See id. at 284.
115. See Khan, 118 S. Ct. at 284.
116. See id.
117. See id. It should be noted that this is not the first time the Court has overruled its own precedent in the area of vertical restraints of trade. In Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977), the Court held that vertical non-price restraints are to be governed under a rule of reason analysis. This decision overruled United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967), which stated that vertical non-price restraints were per se illegal. Thus, the Court is not adverse to changing its judicial mind when economic experience indicates previous decisions were misguided.
The *Khan* decision appropriately brings the focus in vertical maximum price fixing cases to the ultimate effect of the activity on the consumer. *Khan* clearly provides manufacturers with the legal ability to engage in promotional activities with wholesalers or retailers which involve maximum price fixing elements.\(^{118}\) For example, sellers can enter into promotional agreements with distributors or retailers which state that the retailers cannot price the product above a certain level. Precedent allowed manufacturers to set up promotional rebates with distributors without fear of violating the per se rule against vertical price fixing.\(^{119}\) However, *Khan* solidified the holdings in these prior cases and firmly establishes a manufacturer's ability to engage in maximum retail price maintenance when the agreement ultimately benefits the consumer.

Unfortunately, *Khan* does not clarify the factors involved in the rule of reason analysis that courts must entertain in vertical maximum price fixing cases.\(^{120}\) However, *Khan* suggests it is likely that federal courts will not invalidate a vertical maximum resale price maintenance agreement unless the court determines that the maximum pricing agreement is masking a minimum price fixing agreement.\(^{121}\)

The argument that the maximum price is really a surrogate for the minimum price is the most probable anti-competitive problem that could arise in the vertical maximum pricing context. In essence, the maximum price agreement is alleged to mask a collusive cartel price. The rule of reason test may inquire as to whether the vertical maximum price agreement displays the reduced output and higher priced characteristics of a cartel.\(^{122}\) If not, the agreement would not violate even a rule of reason analysis. In more general terms, one commentator predicts that a vertical, maximum price-fixing restraint should pass the rule of reason test if vigorous interbrand competition\(^{123}\) is sufficient to prevent the supplier from raising prices and reducing output. Most programs and agreements which attempt to respond more efficiently to market forces will be legal, whereas efforts by suppliers to use their market power to distort the market forces may be in legal jeopardy.\(^{124}\)

A recent case decided after *Khan* which applied the rule of reason to an alleged vertical maximum price fixing agreement is *All Care Nursing Services, Inc.*, v.

\[^{119}\] See, e.g., Acquire v. Canada Dry Bottling Co., 24 F.3d 401 (2d Cir. 1994); Jack Walters & Sons Corp. v. Morton Bldg., Inc., 737 F.2d 698 (7th Cir. 1984); AAA Liquors, Inc. v. Joseph E. Seagram & Sons, Inc., 705 F.2d 1203 (10th Cir. 1982).
\[^{120}\] See SILBERMAN, supra note 118, at 145.
\[^{121}\] See *Khan*, 118 S. Ct. at 283.
\[^{122}\] See EASTERBROOK, supra note 63, at 901-04.
\[^{123}\] See Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 52 n.19 (1977) ("Interbrand competition is the competition among the manufacturers of the same generic product... and is the primary concern of antitrust law... In contrast, intrabrand competition is the competition between the distributors wholesale or retail of the product of a particular manufacturer.").
\[^{124}\] See SILBERMAN, supra note 118, at 145.
High Tech Staffing Services, Inc.\textsuperscript{125} In \textit{All Care}, the Eleventh Circuit addressed an alleged vertical maximum price fixing agreement between a group of hospitals and a number of temporary nursing agencies. The \textit{All Care} court held that a vertical agreement which prevents rising prices will pass the rule of reason test outlined in \textit{Khan} if the agreement remains responsive to market forces.\textsuperscript{126}

In \textit{All Care}, twelve hospitals in southern Florida solicited bids from temporary nursing agencies as part of a Preferred Provider Program (PPP). The nursing agencies selected became preferred providers of nursing services to the member hospitals. Under this joint buying arrangement, the hospitals were obligated to utilize nurses from preferred provider agencies before seeking nurses from nonpreferred provider agencies. Each hospital entered into individual contracts with the preferred agencies. One of the contractual provisions stated that the preferred agencies could not raise the prices for nursing services during the length of each contract — one year. However, each agency could utilize a provision in the contract called an "escape clause." Each agency could take advantage of changing market conditions by terminating its contract with a particular hospital upon thirty days notice. The agency could then sell its nursing services to member hospitals or other purchasers of nursing services for higher prices.\textsuperscript{127}

The \textit{All Care} court noted that the agreement in dispute was a vertical arrangement which stabilized the prices for nursing services to a certain degree.\textsuperscript{128} However, the court cited \textit{Khan} for the proposition that vertical arrangements which prevent prices from rising above a certain level are no longer per se illegal.\textsuperscript{129} Consequently, the court applied a rule of reason analysis to the agreement. The court determined that the agreement was not inherently anti-competitive.\textsuperscript{130} Although the agreement tended to stabilize prices, the "escape clause" allowed the competitive market to determine prices.\textsuperscript{131} Thus, this particular arrangement did not violate section 1 of the Sherman Act.

The outcome in \textit{All Care} is consistent with other recent cases which cite \textit{Khan}.\textsuperscript{132} Plaintiffs challenging vertical maximum price fixing agreements are now faced with an extremely difficult task. The plaintiffs must now demonstrate that the effect of the agreement is to damage competition in the relevant market and that no corresponding pro-competitive justifications for the agreement are present. It would be foolish to state that a plaintiff will never win a rule of reason case in this context; however, since \textit{Khan}, the reported cases indicate that no plaintiff has won a pure vertical maximum price fixing case analyzed under the rule of reason.

\textsuperscript{125} 135 F.3d 740 (11th Cir. 1998).
\textsuperscript{126} See id. at 748.
\textsuperscript{127} See id. at 744.
\textsuperscript{128} See id. at 747-48.
\textsuperscript{129} See id. at 748.
\textsuperscript{130} See id.
\textsuperscript{131} See id.
\textsuperscript{132} See, e.g., Mularkey v. Holsum Bakery, Inc., 146 F.3d 1064 (9th Cir. 1998).
B. State Oil Co. v. Khan — Reflecting Current Trends in Antitrust Law

*Khan* provides two key insights into general trends in antitrust law. First, *Khan* reinforces the judgment of the Supreme Court that per se rules in general should be utilized only when the activity in question has been demonstrated to be particularly pernicious.133 During the 1960s, the Court established per se rules for vertical restraints of trade without any economic proof, either practical or theoretical, that vertical restraints of trade are inherently detrimental.134 However, the *Khan* Court recognized that the economic evidence indicated that vertical maximum price fixing actually increases interbrand competition and reduces prices paid by the consumer.135 After *Khan*, the per se standards as outlined in *Northern Pacific Railroad* once again retain their vitality. Second, the case reinforces the limited force and effect of stare decisis in antitrust law. Although some may be concerned with the lack of settled law, it is entirely appropriate that cases which over time prove to be inflexible and unwieldy are reevaluated and perhaps overruled. Antitrust law to a large degree is the product of current economic theory. Because of the changes in knowledge over time, judges must have the tools to change the law to reflect the changes in empirical observations. The *Khan* Court firmly established its capacity to engage in a detailed economic analysis to determine the effects of certain agreements on competition itself, and not individual competitors. The purpose of the Sherman Act remains intact.

VI. Application of Khan to Oklahoma Law

Oklahoma has recently revised a majority of its antitrust laws which were first enacted in 1910. The Oklahoma Antitrust Reform Act (the Act) became law on July 1, 1998.136 The main purpose of the Act is to align the Oklahoma Antitrust laws, as nearly as possible, with Federal Antitrust law.137 As such, the analogous Oklahoma Antitrust laws are to be interpreted consistently with the federal case law interpreting section 1 of the Sherman Act.138

The Act clearly indicates that vertical maximum price fixing cases brought by a plaintiff under the applicable Oklahoma law will be affected by *Khan*. Vertical maximum price fixing cases will be analyzed under a rule of reason analysis consistent with *Khan* and other federal court decisions interpreting *Khan*. Oklahoma is extremely fortunate that the rule of reason analysis has replaced the

134. *See*, e.g., *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967) (holding that vertical non-price restraints were per se illegal).
137. *See* id.
per se rule in vertical maximum price fixing cases due to a quirk in the Oklahoma statute analogous to the Sherman Act.

Section 203(A) of the Oklahoma Antitrust Reform Act is analogous to section 1 of the Sherman Act. Section 203(A) provides in pertinent part: "every act, agreement, contract, or combination . . . , or conspiracy in restraint of trade . . . is hereby declared to be against public policy and illegal." As written, this section appears to differ in one respect from section 1 of the Sherman Act. Section 203(A) contains the word "act" in addition to the other language which mirrors section 1 of the Sherman Act. In Harold's Stores, Inc. v. Dillard Department Stores, Inc., the Tenth Circuit interpreted this section to extend beyond the purview of the Sherman Act. The Tenth Circuit held that unilateral as well as concerted behavior which unreasonably restrains trade is illegal under Oklahoma law.

As a consequence of this interpretation, a plaintiff attempting to bring a vertical maximum price fixing claim under the applicable Oklahoma statute before Khan possessed two advantages. First, of course, the plaintiff could attempt to utilize the per se rule as outlined in Albrecht. Second, the plaintiff need not have shown an "agreement" to fix vertical maximum prices. Section 203(A) merely requires proof of a unilateral act, not proof of concerted action. Therefore, under Oklahoma law, a manufacturer could be liable for unilaterally imposing vertical maximum price restraints even if there was no agreement to fix a maximum price.

After Khan, vertical maximum price fixing cases brought under section 203(A) of the Act will not receive per se treatment but will be judged under the rule of reason. Consequently, it will be much tougher for Oklahoma plaintiffs to win this type of antitrust lawsuit. How the Oklahoma courts will sculpt a rule of reason analysis for vertical maximum price fixing cases brought under the Act remains open to question. However, Oklahoma precedent suggests these plaintiffs will face many difficulties. Oklahoma courts have not issued decisions favorable to plaintiffs in other types of vertical restraint cases judged under the rule of reason in the recent past.

VII. Conclusion

This note proposes a causal link between the Albrecht decision and the decreasing number of independent retailers of gasoline in Oklahoma. Albrecht

139. 79 OKLA. STAT. § 203(A) (Supp. 1998).
140. 82 F.3d 1533 (10th Cir. 1996), cert. denied, 117 S. Ct. 297 (1996).
142. See Harold's Stores, Inc., 82 F.3d at 1550.
created incentives for businesses to vertically integrate operations, thus lessening the need for independent retailers of gasoline. It is safe to say that significant changes in the retail gasoline industry have occurred during the last thirty years. Integration and consolidation are words which highlight this transformation. Undoubtedly, this transformation did not occur solely because of the *Albrecht* decision. A variety of factors have influenced the current state of affairs. However, the *Albrecht* rule certainly played a part in the increasing vertical integration of brand name gasoline retailers in Oklahoma.

*Khan* will not rectify in one swoop the wrongs created by the *Albrecht* decision. What is done cannot be undone. However, *Khan* is a step in the right direction. Antitrust policy in the context of vertical maximum price restraints should continue to focus on the dual aims of promoting competition and increasing consumer welfare.

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