

Establishing and Maintaining an Effective Minimum Resale Price Policy: A Colgate How-To

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FEATHERY GOLF COMPANY MANUFACTURES PREMIUM GOLF EQUIPMENT. Through extensive research efforts, the company has developed a new premium golf ball that provides an explosive, high launch for maximum airtime and a high spin rate—hence its trademark, Launch Control®. Feathery's President is concerned that once distribution is expanded to off-course golf specialty shops, Internet retailers, and mass merchandisers, significant discounting will occur and retailers will place pressure on the company to reduce its prices to them. Such discounting would detract from the premium image of Launch Control golf balls, lead to claims of inferiority by tour professionals not sponsored by Feathery and make further investment in new golf equipment technology unattractive to the company. According to Feathery's finance and market research departments, the Launch Control ball must be sold at retail for at least \$60 per dozen to achieve the correct market positioning and to recover the company's investment. The Division President asks you, as Feathery's antitrust counsel, for advice on how to lawfully achieve this pricing objective. Where do you begin?

Significant discounting of a product can adversely affect the manufacturer, its resellers and the product itself by eroding brand image, jeopardizing the manufacturer's ability to invest in new technology and product improvements, and discouraging the provision of desirable pre- and post-sale customer support services.¹ An increasingly popular way to address these concerns is through the implementation of so-called "Colgate policies"—whereby a supplier, without reaching an agreement, suggests a minimum or exact resale price and refuses to make further sales to any reseller that does not comply.² Indeed, many well-known manufacturers have adopted these policies successfully in such diverse industries as consumer electronics, furniture, appliances, sporting goods, luggage, handbags, agricultural supplies, and automotive replacement parts.³

While a resale price policy is not a panacea, it can be a powerful and effective tool to curb discounting. Provided that such a policy is carefully designed, implemented, and applied,

the legal risk is sufficiently low so as to be acceptable to many companies. The notion that this area is an antitrust minefield is largely driven by high-profile government enforcement efforts against suppliers that knowingly, recklessly, or ignorantly used defective policies, applied them in a sloppy way, or otherwise reached illegal agreements on minimum resale prices.⁴ The fact remains that, with little fanfare, many companies have employed resale price policies for years, and new ones have been adopted that achieve the desired results. Indeed, successful policies rarely get attention, except, perhaps, in limited-distribution trade publications. Although no statistics exist on this issue, our experience suggests that there are far more lawful policy successes than illegal failures.

Based on the Supreme Court's language in *Colgate*, resale price policies initially may appear simple to draft and implement. However, much like peeling an onion, their complexity only becomes apparent when the work begins and the layers of real world relationship intricacies must be taken into account. *Colgate* policies are much more than a one-paragraph, lawyer-drafted piece of paper sent out to resellers at the whim of a corporate executive. They involve the delicate implementation of a complex business strategy and program that carries substantial legal and business risks if not done right.⁵

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In the more than eighty years since the *Colgate* decision, there is surprisingly little, if any, practical written guidance to counsel companies considering the adoption of such policies.⁶ Based on our collective experience in drafting, implementing, and applying many successful resale price programs in a wide variety of industries, this article attempts to help fill that void.

When Does a Resale Price Policy Make Sense?

Faced with what they deem as unacceptable discounting on the part of resellers, suppliers typically wish to influence resale prices for one or more of the following reasons: (1) protect reseller margins so that desirable pre- and post-sale services and infrastructure can be provided;⁷ (2) support brand image (usually a premium positioning) by, among other things, avoiding its use as a loss leader; (3) insure appropriate price levels to facilitate technology development and new product introductions; and (4) level the reseller playing field to avoid destructive channel conflict.⁸ Historically, suppliers either simply raised prices to resellers in the hope that resale prices also would move upward or they carefully selected and retained resellers that did not unacceptably discount. Other common methods include minimum advertised price (MAP) programs, target price rebates, and direct dealing by the supplier with consumers or end-users.⁹ However, the shifting bargaining power that goes with reseller consolidation and the increased importance of brand positioning, as well as the price transparency of the Internet and the shopping for discounts it encourages, have made the use of minimum resale price policies more attractive.¹⁰

Internal Business Considerations. In contemplating whether to adopt a *Colgate* policy for one or more products, a pivotal component for success is widespread support and acceptance throughout the supplier's organization, beginning with senior management and including everyone who has contact with affected resellers.¹¹ As long as proper steps are taken, the legal risks associated with a *Colgate* policy generally are well within a range most business people would find acceptable. At the same time, such a policy certainly is more aggressive than alternatives like MAP programs and therefore may conflict with the supplier's appetite for legal risk or its tolerance for trade relations risk, particularly if the supplier is conservative by nature or is uncomfortable with adopting what essentially is an ultimatum to resellers and actually refusing to do business with those that fail to comply.¹² It also may conflict with the supplier's corporate culture of dealing with resellers in an "easy-to-do-business-with" mode or an "open-door/discuss-anything" manner. Designing and implementing *Colgate* policies require serious commitment and rigor on the part of the supplier. If either is missing, the program is condemned to failure and the legal risks soar.¹³

External Business Considerations. A minimum resale price policy is most likely to be effective if the covered products have brand power, i.e., they have a strong identity and are highly desirable based on quality or other unique or

attractive features.¹⁴ If a supplier were to adopt a *Colgate* policy for a product lacking such power, it is probable that a reseller would simply substitute a product from another supplier or even one sold under the reseller's private label. Similarly, a supplier cannot implement a pricing policy as a revenue prop for an inferior product, as customers will simply choose alternatives. At the same time, there usually is a correlation between the perceived value of a strong brand and reseller willingness to discount it by promoting that the reseller sells the well-known product for less. In other words, the very attractiveness of a product that makes it susceptible to discounting also typically makes it a good candidate for an effective minimum pricing policy.

Likely reactions by competing suppliers and resellers also must be considered. For example, other suppliers may encourage a reduction in the resale prices for their products in an attempt to increase market share. In addition, even with brand power, resellers may balk at a policy that establishes an unrealistic resale price, so it is imperative that the supplier thoroughly understands the market and the demand elasticity for the subject products. Perhaps another concern is whether resellers have sufficient inventories of the covered products to enable them to undermine an unpopular policy until the refusal of the supplier to fill new orders for violators catches up with them.¹⁵ Of course, it is not uncommon for at least some resellers to welcome or even encourage the adoption of *Colgate* policies.¹⁶ Finally, reactions of consumers or end-users must be anticipated if they are aware or become aware that the supplier's product is covered by a policy.¹⁷ If the supplier fails to gauge brand strength accurately, use the appropriate minimum price, and accurately predict the reactions of competitors, resellers, and others, it will have engaged in an interesting, but costly, experiment.

What Are the Elements of a Successful Price Policy?

As with any major business strategy, careful planning of a resale price policy increases its likelihood of success. There are five elements to a well-designed policy: (1) an unambiguous business rationale; (2) the description of the scope of the policy; (3) identification of the consequences of a policy violation; (4) analysis of the structure of the current distribution system and, if necessary, undertaking modifications to accommodate the policy; and (5) consideration of ancillary, but important, issues. The supplier's approach to each of these elements greatly impacts how the policy is viewed by the supplier's resellers and its own employees. These are not just good things to consider, but fundamental parts of the business strategy contained in the policy program.

Unambiguous Business Rationale. Many effective policies originate with the goal of establishing or protecting the equity and market position of an exceptional brand or product. There is little incentive for a company or its resellers to spend substantial marketing and development money on new high-quality products only to see them discounted drastically by free-riding resellers, something which also sends

unintended and inconsistent marketing messages to potential consumers or end-users.¹⁸ The price to the ultimate customer of the product, along with the brand name, is one of the key measures used to determine product quality. The names Sony, Rolex, and Mercedes convey much more than the general concept of electronics, watches, and automobiles. If a company is going to continue producing high-quality products and expect its resellers to provide exceptional customer purchasing experiences and services, it may legitimately decide that it needs the assurance of minimum reseller margins to justify the investment and induce reseller support.

A solid, genuine business rationale additionally establishes appropriate internal commitment to implementing and enforcing the policy and provides a clear foundation upon which the company is willing to stand if questioned by the trade press and industry analysts. The rationale must be strong enough that the supplier would have no concern with it appearing publicly. Indeed, a pro-active public relations program may be advisable to address trade relations issues or consumer or end-user perceptions, particularly in those industries that have not seen resale price policies before or where there is a significant risk of backlash.

The Scope of the Policy. There are a host of questions to be considered when evaluating policy scope. Should the policy apply to just a single product, an entire product line, all products of a particular brand, or all of the supplier's products? Should it cover all resellers across the United States or only resellers in particular geographic areas? Should it apply to all distribution channels or just to one or more, like the Internet? The scope of the policy must be customized to achieve the stated business objective in light of the practical issues of enforceability and effectiveness.

A critical issue is picking the right floor price for each of the covered products that strikes an appropriate balance among the marketing goals of the supplier, the demand elasticity for each product, and the realistic margin needs of its resellers.

The Consequences of a Policy Violation. Perhaps the single most critical factor bearing on policy effectiveness is a clear and unequivocal statement regarding the consequences of a violation of the policy. Under *Colgate*, the cautious supplier has but one choice with respect to violators—immediate termination of product purchasing privileges with no warnings, no second chances, and no continued shipments in response to assurances of future compliance—regardless of the size of the violator and the volume of its purchases.¹⁹ Indeed, this requirement has resulted in much nail biting on the part of supplier executives over the prospective loss of substantial business. Warnings, second chances, or some form of economic punishment (e.g., denial of access to other product lines, “lost” orders or late shipments) all significantly raise the level of legal risk by providing the opportunity for the supplier and the reseller to reach an agreement regarding the reseller's future pricing or at least foster the notion that

some sort of quid pro quo was involved. Moreover, economic punishment can be a means to coerce an agreement.²⁰

Most policies state that a violation will result in indefinite lack of direct access to one or more of the supplier's products or imply such duration through silence.²¹ Others may state that the reseller's access is denied for some defined period. The policy must not contain any reinstatement provision that requires express or implied assurances from the reseller regarding its future intentions to adhere to the policy. Thus, to avoid an inference of an agreement with a reseller, reinstatement of purchasing privileges, if allowed, should be objectively-based and available to all resellers on a non-discriminatory basis.²²

Distribution System Analysis. In order to be lawful under *Colgate*, resale price policies must be unilaterally imposed. As a result, the supplier can only apply the policy one level down in a distribution channel. If the supplier sells the products subject to the policy only to resellers directly (sometimes called “one-step distribution”), the one-level-down issue is of no concern. However, if the supplier sells the covered products to some or all resellers through a wholesaler or other intermediary (“two-step distribution”), policy implementation requires some careful thought.²³

Due to the requirement of unilateral action, a manufacturer cannot lawfully agree with a wholesaler that the latter will either apply and enforce the manufacturer's policy with downstream resellers or that it will impose a policy of its own.²⁴ Nevertheless, there are several alternative ways to handle two-step distribution depending upon business needs and supplier capabilities.

1. Apply the Policy Only to Firms that Purchase Directly from the Supplier

(a) *Only to Resellers*—Here, the policy covers only direct-buying resellers, so those that purchase from wholesalers would not be subject to it. Such an approach could be effective if indirect-buying resellers are not discounting or if only a relatively small volume of sales were made through two-step distribution.²⁵ Otherwise, the policy likely would be too porous to be effective.

(b) *Same Policy for Resellers and Wholesalers*—A variant on the previous approach is to recommend a minimum resale price irrespective of the position of the reseller in the distribution channel. In this case, both the direct-buying reseller and the direct-buying wholesaler are subject to the same floor price. Consequently, the supplier influences the resale pricing of those that buy from the wholesaler only indirectly by providing a minimum price to the wholesaler that, when combined with the indirect-buying reseller's margin requirements, hopefully will maintain a rough parity with the prices charged by direct-buying resellers.

(c) *Different Policies for Resellers and Wholesalers*—Another variation is the use of two policies—one for direct-buying resellers and another for direct-buying wholesalers—in an effort to better address the differences between one- and two-step distribution. However, as before, the indirect-buy-

ing reseller's resale price is only indirectly influenced. Moreover, while this option is theoretically possible, it is difficult to recommend a resale price to wholesalers so that, with the addition of the indirect-buying reseller's margin, the resulting resale price is consistently close to the price charged by the direct-buying reseller.

In any of these situations, resale of the covered product at prices even slightly below the recommended resale price may cause destructive channel conflict and raise questions regarding discriminatory policy enforcement. These alternatives also can send inconsistent signals to consumers or end-users.

2. Recast Wholesalers as Agents of the Supplier. The distribution system could be modified so that indirect-buying resellers have a direct relationship with the supplier for each of the products covered by the policy.²⁶ Wholesalers can be recast to act as sales and delivery agents (being paid a commission to cover selling, warehousing, and delivery expenses, as well as profit) either by handling the covered products on a consignment basis (where the supplier carries the inventory on its books) or, at the time of the reseller order, selling the relevant covered products back to the supplier out of the wholesaler's inventory. In this fashion, all resellers become direct purchasers, even those serviced by wholesalers.

With this option, the supplier must recognize that it is stepping into the shoes of the intermediary with respect to what otherwise would be wholesale sales and thus will be required to organize a direct account relationship, including the provision of credit for its many new direct-buying customers (or, to reduce the credit risk, processing their purchases through the use of third-party credit cards). Of course, any such modification to the distribution system will require complete documentation of the new relationships with wholesalers and resellers.

3. Authorize Wholesalers to Resell Only to Certain Resellers. Under this alternative, the supplier enters into written distribution agreements with each direct- and indirect-buying reseller, as well as with each wholesaler. The authorized reseller agreement covers such things as the reseller's use of the supplier's trademarks and appropriate business practices relating to the resale of the supplier's products, while the wholesaler agreement, among other things, permits the wholesaler to sell only to authorized resellers. Although the supplier issues a *Colgate* policy to each reseller, the reseller and wholesaler agreements are silent on this issue. If an indirect-buying reseller violates the policy (or breaches the authorized reseller agreement), the wholesaler is notified that its customer has lost its authorization for one or more products and can no longer be sold it or them.²⁷

Other Important Considerations. Certain factors may operate as an impediment to the use of a resale price policy. For example, the supplier must determine whether there are any contractual constraints to be addressed in drafting or implementing the policy. Do the terms of a written distribution agreement require the supplier to sell all of its products to the reseller? Is there anything else in the contract that

would prohibit or limit the use of a resale price policy? Conversely, does the distribution agreement require the reseller to comply with all policies issued by the supplier? If so, that provision will have to be removed from the agreement prior to adoption of a resale price policy to avoid back-dooring an agreement to set resale price.

Counsel for the supplier also should consider whether franchise, distributor, or dealer protection or other industry-specific laws affect the ability of the supplier to refuse to continue supplying the covered products to the reseller in the event of a policy violation.²⁸ In addition, if the product involved is essential and unique to competition with the supplier in a related market where the supplier has market power, these factors may limit its ability to refuse to deal with a reseller.²⁹ Finally, certain industry-specific laws simply may prohibit the supplier from interfering with resale prices.³⁰

How Should a Resale Price Policy Be Communicated?

It is critical that the resale policy document be carefully crafted so as to provide no opportunity for misinterpretation by resellers or the supplier's employees. Moreover, the more unambiguous the policy, the less opportunity for discussions between the supplier and resellers that could convert the policy into something other than unilateral. While other elements may be necessary to address issues in particular circumstances, the following are the primary points that must be addressed:³¹

Policy Rationale. It may be helpful to include a paragraph setting forth the supplier's rationale for adopting the policy. While not mandatory, a clear and legitimate business explanation for the policy can aid reseller understanding and support.

Policy Coverage. The policy must describe each of the products covered, the resellers or distribution channels to which it applies, and the geographic areas involved. It also must include a policy effective date.³²

Recommended Resale Price. The policy must clearly set forth the recommended minimum resale price for each of the covered products and expressly define each advertisement, offer, or sale below such price to be a policy violation. The policy should also make clear that resellers are free to advertise or sell the product at any price they deem appropriate, but that the supplier will unilaterally enforce its policy.

Definition of "Price." The supplier must also consider how each covered product is sold to the consumer or end-user and address the policy implications of alternative methods by which resellers may offer the product. Should the value of "free" delivery or installation be included in the resale price of the product? How is the resale price determined if the reseller bundles the covered product with other related products and services? Should the product be excluded from "store-wide-10-percent-off sales" or first-time-credit-card-user discounts? What about discounts associated with fre-

quent purchaser cards or discounted sales to employees of the reseller? The supplier must design the policy with an eye toward how the sales behavior of resellers may inadvertently circumvent the policy or purposely game the supplier's program to gain a competitive market advantage or thwart policy operation. The credibility of the supplier and its policy depends greatly on uniform understanding and application of the policy.

Policy Violations. The policy must clearly describe the consequences when a reseller chooses not to follow the policy—the supplier will immediately and unilaterally refuse further shipments. But what happens to the reseller's inventory? The supplier may wish to consider a provision granting it the option to repurchase such inventory in the event of a violation so as to minimize market disruption caused by sales that are almost certain to be below the floor price. To assist the supplier's enforcement efforts, the policy may include an affirmative obligation on the reseller to maintain point-of-sale (POS) transaction records and the right of the supplier to retain an independent auditor to review such records.³³

Policy Modifications. The supplier should include language that makes it clear that the supplier may at any time modify, suspend, or discontinue the policy in whole or part or designate promotional periods during which the terms of the policy change or are inapplicable. This ability reinforces its unilateral nature.

Antitrust Disclaimer. The policy must include unambiguous language stating that the supplier is not seeking agreement from any reseller to adhere to the policy and that it is entirely within the reseller's discretion whether to comply with the floor price. While the policy might also state that resellers are not to report any policy violations (so as to minimize the appearance of supplier/reseller collusion with respect to another reseller), such provisions are not required and, more importantly, have almost no effect.³⁴ In all likelihood, the supplier will get flooded with reports of violations regardless of such language. At the same time, some suppliers rely on such reports to find violations, although a number of such complaints inevitably will prove to be untrue when investigated.

Contact Information. The policy should include the name and contact information of the supplier's designated policy administrator as the person to deal with questions, comments, and complaints.³⁵

Supplementary Materials. Separate from the policy document itself, many suppliers have found it effective to issue the policy with a frequently-asked-questions (FAQs) document which raises and answers policy-related questions most likely to be posed by resellers. Such a document provides consistent answers and avoids discussions regarding the policy with resellers. Creating FAQs during the policy-drafting phase has the added benefit of highlighting policy application issues that might otherwise not have been considered.

How Can a Supplier Successfully Implement and Apply a Resale Price Policy?

A *Colgate* program is much more than a well-crafted policy statement mailed out to resellers. The policy language is only a small part of a well-designed strategy required to insure its success. The reputational costs of an ineffective policy and the legal expenses associated with an unlawful program can be significant, so as little as possible about the policy should be left to chance. The supplier must be committed to the policy from the top down, must carefully coordinate the program, and must provide realistic employee education. Externally, the organization must be perceived by resellers and other market participants as determined, credible, and non-discriminatory. While a successful program can require months of planning, the benefits to the supplier, the brand, and the covered products can be enormous.

Internal Considerations. Given the complexity and the need for considering multiple interests, the development and implementation of a resale price policy should be managed by a small group of marketing, sales, finance, and legal personnel. In addition to investigating the implications of and crafting the policy, this team must establish: (1) the structure for policy administration, (2) a policy operations plan, and (3) an employee education plan.

1. Who Administers the Policy? The supplier's internal administration of the policy should be centralized to assure uniform application, as well as consistent reporting to senior management. The designated policy administrator, preferably a business person with extensive knowledge of the customer base, is the company's "face" with respect to all policy matters. The designation of a senior executive for this role evidences the company's commitment to implementing and enforcing the policy. It is critical that the designee have the authority or be a part of a small team with the authority to make all policy application decisions. The role of such executive or team is to: (1) insure that all policy documents are consistent with the supplier's objectives; (2) effectively communicate the policy to resellers and, as necessary, to others; (3) coordinate employee education; (4) answer policy application questions; (5) conduct investigations and audits; and (6) make all enforcement decisions.

Use of an inter-disciplinary team assures the inclusion of the perspectives of sales, marketing, and finance in all policy-related decisions. In addition, it is critical that antitrust counsel, whether inside or outside, be assigned to work closely with the administrator or the administration team. In the early stages of policy implementation, it is not uncommon for teams to meet several times each week to consider issues that arise during implementation, but that could not realistically have been foreseen in the planning process.

2. How Are Policy Violations Discovered and What Happens Next? Either the policy administrator or the administration team should develop a complete internal policy operations plan. The plan should contain written protocols

for centralizing and handling unsolicited reports of policy violations, conducting investigations, defining the process to be used in determining whether a violation of the policy has occurred, and communicating decisions to resellers regarding the policy. To maintain credibility and avoid unacceptable legal risk, the policy must be enforced uniformly and fairly, and the establishment of written guidelines substantially aids in this effort. Additionally, a policy violation investigation form should be developed to track information regarding alleged violations, including receipt of unsolicited reports of violations, descriptions of investigative steps (such as supplier mystery shops or calls,³⁶ review of advertisements and invoice audits), recording of decisions made and copies of all purchase authorization withdrawal notices.

Given the market advantage that intentional policy violators can have over those resellers that have chosen to follow the policy, the policy administrator's fax machine will hum with the receipt of copies of advertisements and invoices of alleged violators. Regardless of whether the policy expressly instructs them not to do so, every reseller becomes a self-deputized informant. Resellers have been known to conduct their own mystery shops and even to cajole violations. Indeed, it is not uncommon to receive doctored invoices from a complaining reseller—designed to create the impression that a competitor is violating the policy—accompanied by a demand that the competitor no longer be provided access to the covered product or products. While the supplier may take comfort that the policy is effective, safeguards for handling such requests are required to avoid even the appearance of an unlawful conspiracy.

It is risky from both a legal and business perspective to rely upon reseller reports of policy violations alone. Many companies establish a verification process that does not involve any confrontation of the allegedly offending reseller regarding its sales practices, but instead uses multiple mystery shops or calls and invoice audits to confirm policy violations.³⁷

Many large resellers (particularly in the consumer goods arena) have thousands of sales employees, and it is inevitable that unintentional pricing errors will occur.³⁸ Moreover, the timing and placement of advertisements is far from an error-free process. Particularly with respect to products that are advertised frequently, inadvertent violations can easily result from printer error and go unnoticed by the reseller. It is not illegal for the supplier to unilaterally determine that a formal policy violation has not occurred where a very small fraction of a retailer's sales appear to be inadvertently below the recommended resale price and do not appear to evidence intentional policy violations. However, the supplier risks creating the potentially policy-fatal perception among resellers that the policy is not being uniformly enforced.

Without having any conversations with the reseller regarding its pricing intentions, the supplier must walk a fine line in unilaterally assessing the retailer's intent and making the policy violation determination. In those cases where the available data demonstrates a possible violation, but does not

provide adequate clear evidence, some companies simply resend copies of the policy (without any further comment or communication). As a rule, it is important to have as many independent sources of data as is feasible and to document all decisions.

To decrease credibility problems with under-enforcement, a number of suppliers create formal policy audit programs. Such audit programs can take several forms. The most informal is a request to company employees to watch and listen for, but not to solicit, reports of policy violations. A more formal program might include the retention of a marketing research company, accounting firm, or detective agency to conduct mystery shops or calls and field audits of reseller records.³⁹ The use of outside auditors assures no communication between business teams and resellers in the audit context and provides an independent source of information with which to make enforcement decisions.

Regardless of the investigatory method used, the process needs to move relatively swiftly to avoid creating any reseller perception that the company is not enforcing the policy. The pressure on resellers to lower their prices to compete with local policy violators is significant and their tolerance in waiting for supplier enforcement actions normally is rather limited. The policy will rapidly fail if sufficient numbers of resellers determine that there is little to be gained by following the policy and little to lose by ignoring it.

The policy administrator must also establish a protocol for communications with resellers regarding violations and updates of the policy. The letter exercising the supplier's unilateral right to refuse to continue selling to confirmed violators must be carefully crafted to avoid any suggestion that the supplier is seeking some assurance of future compliance. The supplier must insist that once the letter is sent, there can be no communication with the offending reseller regarding the violation or the reseller's willingness to bring its prices to the level desired by the supplier.

A difficult issue that should be resolved prior to implementation is whether, and at what time, the supplier will unilaterally offer a reseller whose purchasing privileges have been revoked the opportunity to begin purchasing the product or products again. Some companies have policies stating that violators will not again be offered the product for resale for a defined lengthy period, such as one year, following termination. Many do not inform customers regarding the reinstatement policy so as to prevent them from attempting to game the policy by placing enough advance orders to support their selling below the minimum prices for a significant period.”

However, under the Sherman Act, reinstatement cannot be linked to any promise by the reseller to comply with the policy in the future. As a result, beyond merely offering the customer the opportunity to once again purchase the product or products (subject to the policy), there must be no communication regarding the reseller's future pricing plans. There is obviously a rather delicate balance between the sup-

Sample Minimum Resale Price Policy

Feathery Golf Company Launch Control® Golf Ball Distribution Policy

Effective January 1, 2004

FEATHERY GOLF COMPANY has determined that in order to better compete against existing premium golf balls and to properly position the Launch Control golf ball in the market, it must exercise a greater degree of control over the distribution of Launch Control golf balls. Therefore, all sales of Launch Control balls will be subject to this Distribution Policy. This Policy has been unilaterally adopted and will be enforced strictly and uniformly.

Although resellers remain free to establish their own resale prices, Feathery will, without assuming any liability, cancel all orders and will indefinitely refuse to accept any new orders from any reseller immediately following Feathery's verification to its satisfaction that such reseller has advertised, offered, or sold any Launch Control golf balls at a net retail sales price less than the minimum retail price established and announced by Feathery from time to time (the "Floor Price").

This Policy applies to first-quality goods only. It does not apply to distressed merchandise and close-outs as clearly labeled by Feathery. This Policy also does not apply during the off-season period of November through January of each year. It may be modified at anytime by Feathery, and the Floor Price may be affected by promotions announced by Feathery or may change during promotional periods designated by Feathery.

The Floor Price effective January 1, 2004, is \$60.00 per boxed dozen, exclusive of all state and local taxes. Feathery Golf Launch Control balls may not be sold in quantities of less than one dozen and may be sold only in one-dozen increments.

Feathery will not discuss any conditions of acceptance related to this Policy, as it is non-negotiable and will not be altered for any reseller. In addition, Feathery neither solicits, nor will it accept, any assurance of compliance with this Policy. Nothing in this Policy shall constitute an agreement between Feathery and any reseller that the reseller will comply with this Policy.

Feathery sales personnel have no authority to modify or grant exceptions to this Policy. All questions regarding the interpretation of this Policy must be directed to the Launch Control Distribution Policy Coordinator at 1-555-LCH-CTRL.

plier's desire for revenues and taking the risk that the once-offending reseller will violate the policy again.

3. What Should Supplier Employees Be Told? The need for comprehensive antitrust and policy education of all relevant supplier employees—that is, anyone who has contact with resellers—cannot be overstated. A Section 1 violation can occur any time a company employee has any conversation with a reseller regarding the policy in which it is expressed or can be inferred that the reseller has agreed with the supplier to follow the policy. Thus, beyond educating company employees of the business rationale for the policy, explaining the terms of the policy (including outlining why the policy is lawful), and carefully covering the antitrust risk, the critical education message to each company employee is relatively straightforward and can be easily understood by all:

YOU HAVE NO AUTHORITY TO DISCUSS THE TERMS OR APPLICATION OF THE POLICY WITH ANY CUSTOMER. YOUR FAILURE TO ADHERE TO THIS RULE WILL AUTOMATICALLY RESULT IN DISCIPLINARY ACTION. ALL CUSTOMER QUESTIONS REGARDING THE POLICY MUST BE DIRECTED TO THE POLICY ADMINISTRATOR.

All sales, customer service, finance, marketing, credit, and management personnel (along with new employees as they join the company) must be given this message repeatedly through group meetings, written guidelines, wallet or pocket cards, e-mail reminders, and the like. Supplier personnel (other than the policy administrator) should never have any communication with any violator regarding termination. Sales people must understand that it is not their job to explain, police, or intervene in the operation of the policy, and that they can be disciplined if they try to do so.⁴⁰ At the same time, the customer service department must be prepared for calls from consumers or end-users with questions as to why they are unable to purchase the product at a discounted price.

External Considerations.

1. How Will Covered Resellers React? Particularly with respect to product lines and industries in which resale pricing policies are uncommon, a supplier introducing a resale price policy will likely be viewed with great suspicion or scorn. Indeed, a common reseller refrain—until they talk to their own antitrust counsel—is: "You can't do that; it violates the antitrust laws."⁴¹ The supplier's communications with customers and the industry must therefore clearly convey the business rationale for the policy, confidence in the legality of the policy, and a determination to apply it in an even-handed fashion.

Suppliers considering resale price policies should recognize upfront that a unilateral decision to adhere to the policy may not be an easy one for some of its resellers. They may view it as the supplier's unwelcomed intrusion in their business operations and simply refuse to purchase the product subject to

the policy. Others may operate on “everyday-low-pricing” models with pre-existing marketing representations to customers that preclude them from placing a margin of more than a certain percentage on the purchase price of the product to the reseller. Suppliers must account for the potential of lost sales to such resellers in evaluating whether to adopt a policy.

While suppliers cannot reduce this burden other than by giving resellers sufficient advance notice of policy adoption (which is a good idea anyway), suppliers should recognize that some resellers may have an enormous employee education effort confronting them if they choose to follow the policy. Large distributors, mass merchandisers, and club stores may have thousands of employees (and often a high employee turnover rate), who need to be educated on the policy, the reseller’s position with respect to the policy, and the implications of their failing to comply with their employer’s decision to adhere to the policy. It is the reseller’s obligation alone to undertake that educational effort. Indeed, it could be a Sherman Act violation for the supplier to take on that role, other than providing copies of the policy and explanatory materials.

The supplier must also anticipate receiving pleas from resellers whose purchasing privileges have been terminated for reinstatement with assurances that they would adhere to the program “if only they were given another chance.” It is critical that the business team understand at the outset that such letters will be received and that the supplier simply has no choice but to continue to refuse sales to that customer. Indeed, once such unsolicited assurances are received, it is questionable whether the supplier can legally ever reinstate

the reseller even if the supplier has an automatic reinstatement plan in place, unless the supplier or its counsel immediately responds to such assurances in writing by refusing to accept them and emphatically stating that they will not be taken into account in the supplier’s unilateral decision making.

2. Should the Supplier Affirmatively Publicize the Policy?

Beyond distributing policy information packets to its customers, some suppliers invite or submit to trade journal interviews relating to the policy. While the interviewees must spend substantial time with antitrust counsel preparing for such interviews, such communications can minimize the cloud of mystery that can surround the policy in its early stages of implementation. To avoid the risk of awkward responses to interview questions, some opt to issue press releases. Such public dissemination of policy information can have the positive effect of decreasing fears over the company’s intentions and conveying the supplier’s commitment to implementation. Antitrust counsel should monitor such communications to prevent any misimpressions.

Conclusion

Minimum resale price policies can be an extraordinarily powerful tool to protect the viability of products, brands, resellers, and suppliers. However, they are complex and time-consuming to develop and may not be practical or effective for every type of product or market. At the same time and while the margin for antitrust error is narrow, the legal risk can be managed to a level that many companies find acceptable through careful policy establishment, implementation, and application. ■

¹ For purposes of this article, a “reseller” is anyone that takes title to a product and resells it for its own account, including such intermediaries as distributors, dealers, and retailers. (While wholesalers also could be resellers, we discuss them separately later, but do not refer to them as resellers to avoid confusion. See *infra* note 24.) Agents, brokers, and sales representatives are excluded not only because they do not take title, but also because they are extensions of the supplier, which typically controls the prices charged. In addition, “supplier” and “manufacturer” are used interchangeably, although an intermediary could function as a supplier to subordinate members of its distribution channel.

² Section 1 of the Sherman Act, 15 U.S.C. § 1, “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.” *United States v. Colgate*, 250 U.S. 300, 307 (1919). Such circumstances may include “suggesting” resale prices, then refusing to do business with any customer that doesn’t comply, as long as there is no agreement on maintaining the suggested price. *Id.* at 307–08; *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 761 (1984). See also Federal Trade Commission (FTC), *Promoting Competition, Protecting Consumers: A Plain English Guide to Antitrust Laws, Frequently Asked Questions* (second question), <http://www.ftc.gov/bc/compguide/question.htm>. Section 1 does not apply because unilateral policies, by definition, do not meet the statute’s jurisdictional requirement of a “contract, combination . . . or conspiracy.” As a result, neither the rule of reason nor the per se test are relevant. However, if an agreement on resale prices were

present, such an agreement would be judged under the rule of reason if it were for maximum resale prices and the per se rule for minimum or exact resale prices. See *infra* note 10. Under state law, there has been no successful challenge to such policies. See, e.g., *Chavez v. Whirlpool Corp.*, 113 Cal. Rptr. 2d 175 (Ct. App. 2002). In the interest of space, our analysis of the development of the law in this area is necessarily brief. For a discussion of *Colgate* and its progeny, see WILLIAM C. HOLMES, *ANTITRUST LAW HANDBOOK* § 2.15 (2003). Note that such policies and vertical price setting in general are unlawful in Canada, Competition Act, R.S.C. ch. C-34, § 61(3) (1985), and in certain other jurisdictions outside the United States.

³ Most policies seem to involve higher-end consumer products (both durables and non-durables), but industrial suppliers also have found them useful.

⁴ Unfortunately, programs that ostensibly are illegal tend to surface primarily in consent orders and decrees, which usually are short on a description of the facts and analysis of the relevant law. See *infra* notes 5 and 13.

⁵ Although not involving a resale price policy, the manufacturer of George Foreman grills is the most recent addition to the list of suppliers that apparently have crossed the line and entered into illegal express or implied resale price agreements with resellers when what was characterized as its minimum advertised price (MAP) program seems to have gone too far. See *State of New York v. Salton, Inc.*, No. 02 Civ. 7096 (LTS), 2003 WL 21254723 (S.D.N.Y. May 30, 2003) (settlement of enforcement action joined by 47 states, the District of Columbia, and Puerto Rico alleging manufacturer coercion by forcing retailers into agreements to fix the retail prices). For additional background, see the Web site of the National Association of Attorneys General (NAAG), which includes the Amended Complaint, the Settlement

Agreement, the Final Judgment and Consent Decree, and other significant documents, at <http://www.naaq.org/issues/20020909-multi-salton.php>. MAP programs are discussed *infra* at note 9.

- ⁶ The authors are aware of no published articles or conference materials that address in depth the practical aspects of the design and implementation of a *Colgate*-permitted policy. Case law in this area is helpful overall, but tends not to address the nuts-and-bolts issues. As previously noted, consent orders and decrees usually present rather limited facts and even a more limited discussion of the law. (A number of relevant orders and decrees are found *infra* at note 13.) Presentations made by government officials are useful for conveying their perspectives, but there are relatively few speeches to consider. Two examples of such presentations are Commissioner Sheila F. Anthony, Vertical Issues in Federal Antitrust Law, Address at the 13th Annual Advanced ALI-ABA Course of Study, (Mar. 19, 1998), transcript available at <http://www.ftc.gov/speeches/anthony/aliabaps.htm>; and Commissioner Christine A. Varney, Vertical Restraints Enforcement at the FTC, Address at the ALI-ABA Eleventh Annual Advanced Course on “Product Distribution and Marketing” (Jan. 16, 1996), transcript available at <http://www.ftc.gov/speeches/varney/varnmg.htm>. Ms. Anthony currently is an FTC Commissioner, while Ms. Varney is not.
- ⁷ Such services and infrastructure may include such things as product demonstrations, repairs, showrooms, highly trained salespersons, and extensive on-site inventory.
- ⁸ Destructive channel conflict occurs when resellers spend so much time fighting among themselves for sales of the supplier’s brand (“intra-brand competition”) that they fail to compete sufficiently with other brands (“inter-brand competition”).
- ⁹ With MAP programs and target price rebates, the reseller receives a financial incentive from the supplier (usually in the form of a rebate or allowance) to advertise prices at or above minimum levels or, in the case of target price rebates, to sell at a specified price or within a price range. Like most promotional programs, reseller participation is voluntary and, for that reason, such approaches are governed by the rule of reason. See 6 Trade Reg. Rep. (CCH) ¶ 39,057 at 41,728 (FTC May 31, 1987)(MAP programs); see also Sony Music Distrib., Inc., [1997–2001 FTC Complaints and Orders Transfer Binder] Trade Reg. Rep. (CCH) ¶ 24,746 (Aug. 30, 2000) (consent order in which five major suppliers agreed to drop their MAP programs, allegedly because they collectively eliminated price competition). Of course, such incentives also are subject to the Robinson-Patman requirements of the Clayton Act, 15 U.S.C. § 13. The voluntary nature of these approaches means that, unless the financial incentives are sufficient, the reseller will refuse them if it can make more profit through the increased volume associated with discounting. Moreover, MAP programs address the advertised price only, so the reseller may pocket the incentive and still sell at a discounted price. In direct dealing, assuming that there are no contractual or regulatory impediments, the manufacturer bypasses the intermediary to negotiate price or sell directly to the ultimate reseller or customer (or converts the reseller into an agent) and thereby sets the price. For a discussion of the various alternatives to affect resale prices, see Eugene F. Zelek, Jr., *The Legal Framework for Pricing*, in *THE STRATEGY AND TACTICS OF PRICING* 376–78 (Thomas T. Nagle & Reed K. Holden, 3d ed. 2002).
- ¹⁰ Although *Colgate* policies can be used to suggest maximum, minimum, or exact resale prices, their primary use is in establishing minimum or “floor” prices. By far the most common business concern in this area is price discounting. In those instances where a supplier believes that resale prices are too high, the Supreme Court in *State Oil Co. v. Khan*, 522 U.S. 3 (1997), provided another tool by holding that the rule of reason, rather than the per se test, applies to agreements that set maximum resale prices. Except for the fact that they allow no pricing variation at all, exact resale price policies are conceptually the same as minimum price policies. After *Khan*, a resale price policy that sets a maximum price is subject to the rule of reason if, due to the way it is implemented or otherwise, the policy steps over the line and becomes an express or implied agreement on resale prices. However, a policy regarding minimum or exact prices that is or becomes an agreement is per se illegal. See, e.g., *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 761 (1984).
- ¹¹ Buy-in at all levels is essential, including the sales force. See *infra* note 40.
- ¹² The conduct of some companies is closely watched due to their prominence, industry, or large market share. While the law permits them to compete, they typically are more cautious about throwing their weight around. Moreover, another risk factor is regulator efforts to narrow *Colgate* or make it go away. For example, in *Russell Stover Candies, Inc.*, [1979–83 FTC Complaints and Orders Transfer Binder] Trade Reg. Rep. (CCH) ¶ 21,933 (1982), *rev’d*, 718 F.2d 256 (8th Cir. 1983), the FTC launched a frontal attack on *Colgate*, but was rebuffed by the appellate court.
- ¹³ While policies can be changed or dropped at any time by the supplier, special deals and secret exceptions tend to support the notion that the policy is based on illegal agreements, rather than being unilateral. There also is the issue of supplier integrity, or as one of our clients has said, “Never implement a program that you are not prepared to enforce against your biggest customer.” A number of consent orders and decrees illustrate the consequences of ignoring *Colgate* or attempting to skirt it and falling into the trap of illegal resale price agreements. See, e.g., *FTC v. Onkyo U.S.A. Corp.*, 1995-2 Trade Cas. (CCH) ¶ 71,111 (D.D.C. 1995) (action for civil penalties for violation of FTC Order, 100 F.T.C. 59 (1982)); *Nine West Group Inc.*, [1997–2001 FTC Complaints and Orders Transfer Binder] Trade Reg. Rep. (CCH) ¶ 24,707 (Apr. 11, 2000); *Reebok Int’l, Ltd.*, [1993–1997 FTC Complaints and Orders Transfer Binder] Trade Reg. Rep. (CCH) ¶ 23,813 (July 18, 1995); *United States v. Playmobil USA, Inc.*, 1995 WL 366524 (D.D.C. May 22, 1995); *Keds Corp.*, [1993–1997 FTC Complaints and Orders Transfer Binder] Trade Reg. Rep. (CCH) ¶ 23,463 (Apr. 1, 1994); *Nintendo of Am., Inc.*, [1987–1993 FTC Complaints and Orders Transfer Binder] Trade Reg. Rep. (CCH) ¶ 22,968 (Apr. 10, 1991). See also *Salton*, *supra* note 5 (multistate enforcement action claiming illegal conduct in implementing and conducting a MAP program for Salton’s George Foreman grills by improper agreements with retailers to fix prices and coercion of retailers beyond a refusal to deal).
- ¹⁴ Prestige products—those that sell better at higher prices because they include status, exclusivity, and personalized customer attention in addition to the physical product—are particularly good policy candidates. Indeed, consistently high prices are a vital attribute of prestige goods and are demanded by consumers or end-users who can conspicuously consume. See George Ackert, *An Argument for the Exempting of Prestige Goods from the Per Se Ban on Resale Price Maintenance*, 73 TEX. L. REV. 1185 (1995).
- ¹⁵ Another factor which may frustrate a resale price policy is the diversion of the covered products from markets where the policy does not apply to places where it does, making it important for a supplier to determine beforehand whether the necessary distribution system safeguards are in place to facilitate a successful resale price policy.
- ¹⁶ In *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717, 726–27 (1988), the Supreme Court made it clear that suppliers may listen to and even take action based on reseller complaints about the prices charged by other resellers, as long as there is no evidence that the supplier agreed on resale prices with the complaining reseller. Of course, the supplier must be careful to avoid becoming part of an illegal agreement among resellers. See, e.g., *United States v. General Motors Corp.*, 384 U.S. 127 (1966) (agreement between supplier and resellers to cut off resellers that support discounting).
- ¹⁷ The plaintiffs unsuccessfully claimed in *Chavez* that Whirlpool’s minimum resale price policy on KitchenAid dishwashers not only violated California’s antitrust statutes, but also was deceptive because its presence was not disclosed to consumers. See *Chavez*, 113 Cal. Rptr. 2d at 178. Of course, sophisticated consumers or end-users may recognize that a pricing policy of some sort is in effect when shopping efforts reveal pricing uniformity or similarity regardless of the reseller or its location, particularly in the Internet age. The likely reactions of other “publics” (such as political or industry activists) also may warrant consideration.
- ¹⁸ Such discounting may place pressure on the supplier to lower its prices to full-service resellers so that they have sufficient margin to compete against the discounters. However, an overall reduction can rapidly cause prices to spiral downward, as long as discounters continue to underprice other resellers. Apart from resale price policies, the supplier could offer the full-service resellers discounts and allowances to compensate them for the valuable services they provide and the discounters do not. However, a price cut

by the supplier or an increase in allowances erodes the supplier's margin, unless it raises prices to every reseller first, then offers the allowances.

¹⁹ See, e.g., *United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960) (unlawful assurances) and the consent orders and decrees cited *supra* note 13. It may be possible to take steps short of cutting the non-complying reseller off at the knees, such as withdrawing advertising support dollars as an initial response to a violation, with the loss of one or more products to follow if the offending conduct continues. However, at least one enforcement official raised the concern that such a so-called "structured termination" offers the opportunity for discussions which could lead to illegal agreements. Varney Speech, *supra* note 6 (citing *Reebok Int'l, Ltd.*, [1993-1997 FTC Complaints and Orders Transfer Binder] Trade Reg. Rep. (CCH) ¶ 23,813 (July 18, 1995) (consent order where, among other things, Reebok was "fenced in" from using such terminations). Nevertheless, the opportunity for discussions alone is not unlawful, and a case, such as *Acquire v. Canada Dry Bottling Co.*, 24 F.3d 401, 411 (2d Cir. 1994) (upheld supplier practice of obtaining confirming wholesaler and reseller signatures on pre-printed forms containing suggested resale prices to be charged by wholesalers), seems to indicate that the supplier may go quite far and still avoid an illegal agreement. *But cf.* *Russell Stover Candies, Inc. v. FTC*, 718 F.2d 256, 260 (8th Cir. 1983) (discussing the "Doric simplicity" required under *Colgate*). Given the uncertainty in the area and the chances for misstep, the one-strike-and-you-are-out approach still is the most prudent.

²⁰ See, e.g., *Simpson v. Union Oil Co.*, 377 U.S. 13 (1964) (control of leases to coerce compliance); *Lowell v. American Cyanamid Co.*, 177 F.3d 1228 (11th Cir. 1999) (coercive pricing incentives); *DeLong Equip. Co. v. Washington Mills Electro Minerals Corp.*, 990 F.2d 1186 (11th Cir. 1993) (threatened termination coupled with secret rebates to a competing reseller to punish plaintiff for non-compliance); *Isaksen v. Vermont Castings, Inc.*, 825 F.2d 1158 (7th Cir. 1987) (threats to "mix up" orders). See also *Acquire*, 24 F.3d at 410 ("[E]vidence of threats of termination or other explicitly coercive conduct that secure adherence to fixed prices is what supports 'a finding of an illegal combination.'"). At the same time, promulgating a resale pricing policy is not considered coercive, and reseller compliance with it alone is not deemed to be an agreement. See *Russell Stover*, 718 F.2d at 258-60.

²¹ The policy may state that its violation results in the loss of the product or products with respect to which the violation occurred, an entire product line, or all of the supplier's products. With respect to the last alternative, see *infra* note 28.

²² Such an approach is easier to defend over one that makes seemingly arbitrary decisions. At the same time, it should be kept in mind that, under *Colgate*, it is within the supplier's prerogative to decide with whom it will deal for whatever reason it deems appropriate, as long as there is no agreement.

²³ This discussion will address only one-step and two-step distribution. If there are more than two layers, the issues become even more complex.

²⁴ *Spray-Rite*, 465 U.S. at 768 n.13; *Parke-Davis*, 362 U.S. at 45-46. For purposes of this discussion, the term "wholesaler" will be used to describe the intermediary that purchases directly from the supplier and sells to certain resellers, referred to here as "indirect-buying resellers."

²⁵ One of our clients addressed the two-step problem with a practical twist on this approach. It sold the covered products only to direct-buying resellers, while selling higher-priced assortments not covered by the policy to wholesalers.

²⁶ See, e.g., *Ozark Heartland Elecs., Inc. v. Radio Shack*, 278 F.3d 759, 762 (8th Cir. 2002) (Radio Shack and Primestar did not engage in illegal price fixing by setting the fees that Radio Shack dealers were to charge when acting as agents for sales of Primestar satellite television systems).

²⁷ Under this option, the supplier remains two steps removed from the sale to the ultimate consumer or end-user. As a result, it may have less ability to monitor and quickly react to sales activity at this level.

²⁸ For example, pulling all the supplier's products in the event of a policy violation may be tantamount to termination of the reseller relationship. Many states have franchise, distributor, or dealer protection laws that restrict the ability of the supplier to do so, although such laws often apply to certain industries only (e.g., motor vehicles, agricultural equipment, and alcoholic beverages). At the same time, some states, like Wisconsin, have statutes

of general applicability. See Wisconsin Fair Dealership Law, WISC. STAT. § 135. To the extent that such laws apply, it may be prudent to continue the relationship with some products, although Wisconsin law also prohibits changing the reseller's "competitive circumstances" without cause. *Id.* § 135.03. Regardless of the presence of protective laws, termination of the business relationship with a reseller may result in litigation. Whether as part of a complaint or a counterclaim and regardless of the merits, a supplier should anticipate that its resale price policy may be called into question and should take every reasonable step to make sure that it will withstand scrutiny.

²⁹ *Compare Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451 (1992) (Kodak's discontinuance of independent repair service access to allegedly unique repair parts may have illegally tied the parts to the repair services market in which Kodak competed) with *Intergraph Corp. v. Intel Corp.*, 195 F.3d 1346, 1357 (Fed. Cir. 1999) (Intel's refusal to continue supplying chips to a customer upheld where such chips were for use in a market where Intel did not compete).

³⁰ For example, a number of states prohibit or appear to prohibit beer suppliers from interfering with the prices charged by their wholesalers. *E.g.*, ALA. CODE § 28-8-3; ARK. CODE § 3-5-1107; TEX. ALCO. BEV. § 102.75.

³¹ Accompanying this article for reference is a simplified policy example labeled "Feathery Golf Company Launch Control Golf Ball Distribution Policy."

³² Adequate advance notice is usually a good idea so that resellers can make appropriate adjustments to their businesses, particularly due to lead times in advertising and catalog production.

³³ Although POS data is historically more readily available for consumer products due to the prevalence of checkout scanners, industrial suppliers are increasingly encouraging or requiring the everyday provision of such data by their resellers.

³⁴ See *supra* note 16.

³⁵ See the next section for a detailed discussion of the role of the policy administrator.

³⁶ A "mystery shop" or "mystery call" is when a supplier or reseller sends a person to visit or call a reseller to determine the price at which a product is offered or sold or other aspects of the way business is conducted. While suppliers may employ this technique as part of enforcing a resale price policy program or otherwise, resellers frequently use it on themselves for quality control purposes or on competitors for comparison.

³⁷ According to the *Chavez* court, "Just as the announcement of a resale price policy and refusal to deal with dealers who do not comply is permissible, measures to monitor compliance that do not interfere with the dealers' freedom of choice are permissible. To hold otherwise would render the manufacturer's announced policy ineffective and undermine rights protected by the *Colgate* doctrine, and could also result in the mistaken and arbitrary termination of dealers. By monitoring the dealers' compliance without forcing compliance or seeking or receiving communication of their compliance, a manufacturer permissibly exercises its right to select with whom to do business and on what terms." 113 Cal. Rptr. 2d at 182-83.

³⁸ By the same token, we know of a situation where a large reseller responded to a resale price policy by denying any responsibility for the sales conduct of its employees. The supplier tactfully rejected this attempt to dodge the policy.

³⁹ Note that some states have statutes containing language so broad that they could be read to require that mystery shops be conducted only by licensed private detectives. See CAL. BUS. & PROF. CODE § 7521; TEX. OCC. § 1702.104.

⁴⁰ Some sales people, particularly those whose compensation is based at least in part on reseller purchases, seem to be susceptible to "Stockholm Syndrome," in which they come to identify strongly with their reseller customers. Controlling what sales people say and their willingness to avoid interfering with the operation of the policy are critically important. Moreover, in some cases, the compensation program may have to be modified.

⁴¹ Sometimes resellers persist in making this claim even after they talk with their counsel.