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Lights Out for Resale Price and Dual Distribution Class Action

On December 2, 2010, the Court of Appeals for the 11th Circuit affirmed a ruling of dismissal entered by the United States District for the Northern District of Georgia. *Jacobs v. Tempur-Pedic Int.'l, Inc.*, No. 08-12720. Plaintiff Jacobs brought an action on behalf of a class of purchasers of "visco-elastic foam" mattresses from defendant Tempur-Pedic North America, Inc. ("TPX"). Jacobs had purchased a mattress from a TPX distributor in Georgia. Pursuant to the TPX distributor's agreement, the distributor sold the mattress to Jacobs at a price equal to or above the minimum retail price required by the agreement. Jacobs then brought a class action for alleged violations of Section 1 of the Sherman Act.

Jacobs alleged two theories of recovery. The first was that the minimum price required by the distribution agreement constituted vertical resale price maintenance in violation of Section 1. The second was that, because TPX sold its mattresses through its own website at the same minimum price, it was a "dual distributor", and had entered into a horizontal price fixing agreement with its distributors, in violation of Section 1.

The District Court dismissed Jacobs' complaint for failure to state a claim upon which relief can be granted under *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007). In affirming, the Court of Appeals noted that its mission was to determine *de novo* whether the complaint contains "allegations plausibly suggesting (not merely consistent with) [a conspiracy or] agreement." In other words, the issue was whether the complaint "possesses enough heft to show that the pleader is entitled to relief." *Twombly* at 557. As a myriad of recent cases confirming dismissals under *Twombly* have attested, the key is "plausibility". Do the allegations "nudge" the claim across the line from conceivable to plausible?" To do so, the complaint must contain more than labels and conclusions and a formalistic recitation of the elements of a cause of action.

The court dismissed Jacobs' complaint for failing to properly allege a relevant market. It noted that people sleep on mattresses in general, and that it would be conclusionary whether "visco-elastic foam mattresses" formed a "distinct" submarket within a larger market of mattresses. Jacobs argued that he should be allowed an opportunity to engage in discovery to demonstrate that, in fact, there is a distinct submarket for visco-elastic foam mattresses within a broader market. Unpersuaded, the Court of Appeals, noted that, in any event, there was no showing that "visco-elastic foam mattresses" could be a proper distinct submarket, as there were no allegations as to anticompetitive impact within this market.

While the Court of Appeals agreed that Jacobs did not have an opportunity to add facts through discovery that would support a specific relevant submarket, this was simply a function of his failure to properly allege plausible facts under *Twombly* itself. Allegations that there was a submarket that was separate and distinct from the market for mattresses is merely a conclusionary statement, and begs the question whether visco-elastic foam mattresses properly comprise a "submarket". It does not add any factual information relating to the cross-elasticity of price, or demand differentials, that would indicate whether consumers considered such mattresses differently then traditional mattresses or whether consumers considered them close substitutes. While the Court of Appeals recognized that there is legal support for the viability of a relevant sub-product market, Jacobs' proposed submarket failed to satisfy the "practical indicia" elements set forth in *Brown Shoe Co., v. United States*, 370 U.S. 294 (1962).

The Court of Appeals then takes the reader upon a trip beginning with the 1911 *Standard Oil* case, announcing a "rule of reason", through the series of cases eliminating or narrowing the use of *per se* rules in antitrust conspiracy cases. We are advised that *Dr. Miles Med. Co v. John D. Park & Sons Co.*, 220 U.S. 373 (1911) rested upon "infirm economic

rationales", and in any event, has been explicitly overruled in *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. H77 (2007).

The court noted that in *Leegin*, it had been generally recognized by advances in economic analysis that the reduction of intrabrand competition in order to further interbrand competition was "procompetitive," as it reduced the threat of "free riding" by discounters, and incentivized increased investment in enhanced services that more effectively sell the manufacturer's products relative to rival offerings. Accordingly, after *Leegin*, a plaintiff bears the burden, under the rule of reason, to establish that it is more likely than not that resale price maintenance engaged in by a manufacturer of a product plausibly restrains interbrand as opposed to intrabrand competition.

One might ask how a plaintiff, such as Jacobs, can be expected to plead nonconclusory facts that visco-elastic foam mattresses are more expensive then traditional innerspring mattresses, and have "unique" attributes that would constitute a properly delineated product submarket? Whatever the answer, the conclusion remains the same. Jacobs loses. However, a "quick look" on the internet under "mattresses" would belie many of Jacobs' conclusory allegations. Mattress ads on the internet indicate a price band from $300 to $5,000. The internet mattress ads depict a veritable continuum of choices presented to consumers. Visco-elastic foam mattresses are positioned as direct competitors with innerspring mattresses, including offerings in numerous configurations, some with foam additives, and individualized firmness memories. But, based upon the allegations contained in the complaint, Jacobs has failed to state a claim upon which relief can be granted. The plaintiff has simply failed to allege plausible allegations that visco-elastic foam mattresses constitute a properly defined antitrust submarket, or that there is any plausible actual or potential harm to competition within such a market.

The remainder of the opinion treats us to a discussion of whether a defendant has engaged in horizontal price fixing as a "dual distributor" where it sells its products on its website at the same minimum price that it requires of its distributors. The court's treatment and dismissal of the horizontal price fixing claim could be summarized as "saying so, doesn't make it so." Courts have generally viewed manufacturer-distributor chains as vertical, and not horizontal in nature. It is just as plausible that the pricing levels were within the individual distributor's economic self-interest. The court concluded that mere parallel conduct is insufficient to warrant an inference of concerted action, where the exercise of individual self-interest is just as plausible, citing *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986).

District Judge Ryskamp, sitting by designation, wrote a stirring dissent. He noted that determining whether a complaint states a "plausible" claim is a context–specific task that requires the reviewing court to draw upon its "judicial experience and common sense". As this will vary, judge by judge, a dismissal without allowing either limited discovery, or leave to the filing of an amended, and more "factually" explicit iteration should be error. Jacobs could not be expected to provide factual allegations of cross-elasticity of demand, or other indications of price sensitivity, absent access to discovery. Thus, Judge Ryskamp would not interpret *Twombly* to require a plaintiff to include "actual evidence" in the complaint, and in any event, would allow liberal amendment thereof.

At the end of the day, however, the lights are out for Jacobs. Sweet dreams.

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