Minimum Resale Price Maintenance Prohibition under the Ethiopian Competition Law: Law and Economic Analysis

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Abstract

Minimum resale price maintenance (MRPM) is a device employed by a manufacturer to control its products after they are sold to retailers. MRPM occurs when a manufacturing firm replaces vertical integration by market exchange to enhance efficiency. Since 1991, Ethiopia has experienced free market economy and enacted competition laws to regulate anti-competitive practices to maximize economic efficiency and social welfare. Previous competition law assessed MRPM under rule of reason to examine economic efficiency; however, the current competition law swerves out of this path and puts MRPM under per se illegal. This Article is a modest contribution to the law and economics analysis and argues that rule of reason approach of MRPM should be adopted rather than making it per se illegal.

Key-Words

Vertical restraint, MRPM, free-riding, efficiency, rule of reason, per se illegal, externality, surplus, experience and credence goods, Ethiopia

JEL-Code

K21, L4, L42

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Introduction

Ethiopia has gone through different economic-transformations characterised by change of economic actors and forms of ownership of resources based on government economic-orientation.[1] Pre-1974, imperial-regime claimed to practice market economy policy-orientation nevertheless with no consolidated competition law. Post-1974, the Dergue-regime, practiced socialist form of economic-system where there was no competition in the market as a matter of ideological-principle.

After the downfall of Dergue in 1991, Ethiopia started experiencing free market economy-policy. The government legislated Trade Practice Proclamation *(*hereinafter referred to as TPP)[2]. Though the TPP lacked comprehensiveness, it intended to establish a system conducive for promotion of competitive environment and regulate anti-competitive practices to maximize efficiency and social welfare as expressed in its preamble. The practices TPP prohibits mirror the Treaty on the Functioning of European Union (TFEU) Articles101 and102.[3] Article 6 of the TPP prohibits price fixing, customer allocation and refusal to deal; however, the Ministry of Trade and Industry may authorize exceptions to these prohibitions under Article 7 as long as "the advantages to the nation are greater than the disadvantages".

In 2010, Ethiopia repealed the TPP and enacted a new law, Trade Practice and Consumers' Protection Proclamation No.685/2010 (hereinafter referred to as TPCPP) that reiterated the government's commitment to a free market economy.[4] Market forces play dominant role in the operation of the market but government intervenes through laws when market fails. This is because pro-competitive economic reforms consisting of

[1] Kibre Moges (2008) 'Policy-Induced Barriers to Competition in Ethiopia', *CUTS International Jaipur*. India, p.3. Available at: http://www.cuts-ccier.org/7up3/pdf/Policy-induced_Barriers_to_Competition_in_Ethiopia.pdf. (Accessed 16 July 2016)

[2] *Trade Practice Proclamation No*. (329/2003) 9th Year No. 49, Addis Ababa 17th April, 2003.

[3] Hussein Ahmed Tura (2013) 'Ethiopian Merger Regulation', Working paper, p.5. Available at: http://dx.doi.org/10.2139/ssrn.2305198 (Accessed 20 February 2016)

[4] *Trade Practice and Consumers' Protection Proclamation No*. (685/2010), Federal Negarit Gazeta, 16th Year No.49, Addis Ababa 16th August, 2010.

liberalization, privatization and deregulation alone are not sufficient.[5] Competition law, which is dubbed as antitrust (antimonopoly law or restrictive business legislation) prohibits various anticompetitive practices. Restrictive business legislation is made to abuse of dominance, anticompetitive practices, mergers and vertical restraints.[6] Among the noticeable lack of explicit recognition of TPP were vertical restraints and mergers.[7]

TPCPP heralded the advent of vertical restraint under Article 13(1(b)) captioned "absolute prohibition" and absolutely prohibits "agreement…in a vertical relationship…object or effect setting minimum retail price". There is exception to this vertical restraint under Article 14 which stipulates

> It is possible for a business person accused of anticompetitive practice as provided for under Article 13(1) (a) and (b) above or other provisions of this chapter, to prove that the technological or efficiency or other pro-competitive gains of the agreement or other pro-competitive gains of the agreement or the concerted practice or the decision by association outweigh the detriments of the prohibited acts.

This mirrors, as it will be discussed, the Chicago school that focuses solely on economic efficiency rather than protection of consumers' interest.

Trade Competition and Consumer Protection (hereinafter referred to as TCCP) has broader goal in relation to competition as Article 3(1) declares its objective to be not only confined to the protection of business from

[5] Kibre Moges Belete (2015) 'The State of Competition and the Competition Regime of Ethiopia: Potential Gaps and Enforcement Challenges', *Organization for Social Science Research in Eastern and Southern Africa* (OSSREA), p.10. Available at www.ossrea.net/images/state_of_competition_ethiopia.pdf (Accessed 20 May 2016)

[6] Harka Haroye. (2008) 'Competition Policies and Laws: Major Concepts and an Overview of Ethiopian Trade Practice Law'. *Mizan Law Review*, **2**(1), p.42.

[7] Hailegabriel Feyissa. (2009) 'European Influence on Ethiopian Antitrust Regime: A Comparative and Functional Analysis of Some Problems'. *Mizan Law Review*, **3**(2), p.285.

anticompetitive behaviour but also to cover promotion of competitive free-market.[8]

TCCP, like TPCPP, contains vertical restraint but with different caption and detail. Under Article 7 with the heading "Anti-Competitive Agreement, Concerted Practices and Decisions" proclaims:

> Any agreement between business persons in a vertical relationship shall be prohibited if: a) It has the effect of preventing or significantly lessening competition, unless a party to the agreement can prove that any technological, efficiency or other pro-competitive gain resulting from it outweighs that effect; or b) It involves the setting of minimum resale price.

The TPCPP under Article 14 prohibits "absolutely" behaviours with the object or effect of "setting minimum retail price" but allows exceptions when there exist technological or efficiency or other gains.

The TCCP emphasizes economic efficiency and allows even horizontal agreement and abuse of dominance as long as efficiency is achieved. However, the TCCP, unlike the TPCPP, doesn't allow exceptions in vertical restraint of minimum resale price maintenance (hereinafter-referred-as-MRPM) even though there is economic efficiency justification. Moreover, non-price-vertical-restraints which have similar effect to MRPM are not prohibited as long as efficiency exists.

The Chicago School placed efficiency at the core of competition law and fiercely attacked the traditional concepts of protecting competitive process or allowing goals of competition law other than efficiency. As a consequence, form-based approach is replaced by effects-based approach, calculating the effects of the behaviour in question on efficiency. In Europe, the transition to an effects-based perspective has been dubbed "more economic approach". The new approach is modelled on the basic assumption that market participants act rationally and maximise their own utility. This effects-based approach has led to a more lenient competition policy, especially in the field of vertical restraints such as MRPM. As observed in legislations, although effect-based approach (rule of reason) is a justification in Ethiopia and the TCCP emphasizes efficiency on a

[8] *Trade Competition and Consumers Protection Proclamation No.* (813/2013) 20th Year No.28, Addis Ababa 21st, Article 3(1),

number of occasions, MRPM is not justified by economic efficiency. As per Article 7(2(b)) of TCCP setting MRPM is prohibited and it is per se (hard core) prohibition. Due to efficiency advantage of MRPM, there is a move to evaluate the MRPM under rule of reason. The main question of this Article is, how efficiency justifies incorporating MRPM under rule of reason than under per se prohibition? It examines and analyzes MRPM from efficiency perspective. Thus, it offers insights of law and economic perspectives to handle issues related to MRPM in Ethiopia. Economic analysis of law involves the application of economic principles and methods to analyze the effects of legal rules. It contains both positive and normative strands. The concept of efficiency is adopted as the criterion for the normative analysis of law and explanatory instrument. The enactments are evaluated whether they advance efficiency and the normative analysis that deals with *the ought to* be of the law to advance efficiency. Taking "efficiency as a legal concern" and justifications from US and EU as hindsight, the Article pleas for repeal of per se MRPM prohibition and making MRPM examined under rule of reason.

The reason to examine US and EU competition laws is not only because Ethiopian competition law is influenced by EU Competition law but also "EU has been exhibiting US approaches in competition law…a change in the US system is likely to indicate a future change in the EU system".[9] Furthermore, as we will examine later, the history of US antitrust law depicts the gradual evolution of strict per se prohibition of vertical restraints to assess under the rule of reason. The evolution in the EU is also promising as competition law has emerged from legal formalism to an effects-based approach that takes into account impact of vertical restraints on economic efficiency.

To meet this objective, this Article is structured as follows. Section one discusses arguments of pro and anti-competitive effect of MRPM. Section two deals with comparative perspective on how MRPM is treated in both US and EU jurisdiction from legal and case analysis. The third section is

[9] Elif Cemre Hazırog˘lu & Semih Gokatalay. (2015) 'Minimum resale price maintenance in EU in the aftermath of the US Leegin decision'. *EUR J Law Econ*, p.2.

devoted to per se and rule of reason. Section four examines MRPM in Ethiopia from economic analysis perspective. Finally, recommendation is provided.

Section 1- MRPM as Double Edged Sword- Anti and Pro-Competitive-Effect

Firms selling their product to retailers want to retain decision-making on how their product is priced, promoted and sold to consumers. MRPM occurs when a firm replaces vertical integration by market exchange to enhance efficiency.[10] Telser expounded that firm uses retailers' service (market-solution) than vertical integration (firm-solution) as long as advantages outweigh disadvantages.[11] There are firms as manufacturer and retailers as distributors. It is intra-brand restraint whereby manufacturing firm regulates retailers conduct to specific brand and no effect on other brand.[12] Hence MRPM is contractual device by which manufacturing firms control retailers' actions as to price and promotion.[13]

The agreement between firm and retailers that the latter will sell goods at agreed price is called resale price maintenance (hereinafter-referred as RPM).[14] The agreed price falls either MRPM (vertical-price-fixing[15]) that allows retailers to sell goods at a price or above a price floor; maximum RPM allowing retailers to sell goods at or below a price ceiling or exact price.[16]

MRPM and maximum RPM make up of vertical restraints as a form of price fixing were classed as per se illegal that they are not permitted under

[10] Roger Blair & David Kaserman (1983) *Law and Economics of Vertical Integration and Control*, Academic Press, New York, p.11.

[11] Lester G. Telser. (1960) 'Why Should Manufacturers want Fair Trade'? *The Journal of Law and Economics*, **3**:86-105, p.88.

[12] Ittai Paldor. (2008) 'The Vertical Restraints Paradox: Justifying the different legal treatment of price and non-price vertical restraints'. *University of Toronto Law Journal*, **58**:317-353, p.317-318.

[13] Howard Marvel & Stephen McCafferty. (1996) 'Comparing Vertical Restraints'. *Journal of Economics and Business*, **48**: 473-486, p.473.

[14] Surinder Tikoo & Bruce Mather. (2011) 'The changed legality of resale price maintenance and pricing implications'. *Business Horizon,* **54**(5):415-423.

[15] Paldor (supra note 12) p.318.

16 Tikoo & Mather (supra note14) p.415-423.

any situation (automatically illegal and defence isn't available).[17] However when time went by, the US Court in *State Oil Co. vs. Khan* ruled that maximum RPM is not per se illegal and passed verdict that it should be assessed under the rule of reason approach whereby all relevant facts peculiar to the restraint should be considered on case-by-case basis. Similarly, the Court in *Leegin Creative Leather Products Inc. vs PSKS Inc.* ruled that MRPM is no longer per se illegal and they should be evaluated under rule of reason. The Court stated that blanket condemnation of bilateral MRPM under per se rule (absolutely illegal) is at loggerheads with economic theory such as consumer welfare.[18] The history of US antitrust regime witnessed evolution of a strict per se prohibition of vertical restraints to assess under rule of reason.

MRPM's swing from per se illegal to be rule of reason and still in some jurisdiction per se prohibition is used because it is considered 'mixed bag' practice having both pro and anticompetitive-effect.[19]

1.1 Anticompetitive Effect of MRPM

1.1.1 Price Increase

Many scholars criticised MRPM because there is immediate price hike of product by retailers; however, with mixed result as to the welfare effect of MRPM.[20] Thomas' empirical survey of RPM depicted more price increase when resale price legalized than the states where resale price remained prohibited.[21] It is empirically confirmed that RPM results in

17 Ibid.

[18] Id.p.416.

[19] Thomas A. Lambert. (2010) 'A Decision-theoretic Rule of Reason for Minimum Resale Price Maintenance'. *The Antitrust Bulletin*, **55**(1):167-224, p.168.

[20] Cemre & Semih (supra note9) p.4.

[21]Thomas R. Overstreet (1983) 'Resale Price Maintenance: Economic Theories and Empirical Evidence', *Bureau of Economics Staff Report to the Federal Trade Commission*. Available at: https://www.ftc.gov/sites/default/files/documents/reports/resale-price-maintenance-economic-theories-and-empirical-evidence/233105.pdf (Accessed 12 May 2016)

price increase and loss of consumer welfare.[22] There is ambiguous evidence for higher price and its effect. RPM doesn't bring price increase and even if it results in price increase it doesn't necessarily harm consumer welfare.[23] Consumers consensually could make trade-off between higher prices and services and information proffered by retailers. Doty asserted price increase only affects infra-marginal consumers who value goods more and continue purchasing at high price whereas marginal consumers would stop purchasing when the price hits high.[24]

1.1.2 Manufacturer Cartel Facilitation

MRPM avoids price flexibility at retailer level and stabilize at manufacturer level.[25] The existence of MRPM makes cheating detection easy or reduces the incentive to cheat for the colluded parties to keep price high. However, this argument is attacked from different fronts. Ippolito examined that there is no empirical evidence to buttress MRPM was employed to facilitate cartels and rather MRPM well-functioned in competitive-market.[26] In similar vein, Thomas asserted that application of MRPM is immensely costly and is not clear MRPM is conducive for "collusive benefit" to the manufacturer.[27] Others also criticised perceived

[22] Alexander MacKay and David Aron Smith (2014) 'The Empirical Effects of Minimum Resale Price Maintenance', *Marketing Series Paper-1-009*. Chicago Booth, p.2. Available at http://ssrn.com/abstract=2513533 (Accessed 20 May 2016)

[23] Andreas P. Reindl. (2010) 'Resale Price Maintenance and Article 101: Developing a More Sensible Analytical Approach'. *Fordham Int'l L.J*, **33**, p.1319.

[24] Ashley Doty. (2008) 'Leegin V. PSKS: New Standard, New Challenges'. *Berkeley Tech. L.J*, **23**:655-684, p.660.

[25] Robert Pitofsky. (1983) 'In Defense of Discounters: The No-Frills Case for a Per se Rule Against Vertical Price Fixing'. *The Georgetown Law Journal*, **71**:1487-1495, p.1490.

[26] Pauline M. Ippolito. (1991) 'Resale Price Maintenance: Empirical Evidence from Litigation'. *Journal of Law & Economics*, **24**:263-294, p.281-282.

[27] Thomas A. Lambert. (2008) 'Dr. Miles is Dead. Now What?: Structuring A Rule of Reason for Evaluating Minimum Resale Price Maintenance'. *William and Mary Law Review*, **50:**1937-2005, p.1949.

risk of cartel facilitation that non-price vertical-restraints might be employed as much as MRPM to meet the collusive outcome.[28]

1.1.3 Retailer Level Cartel Facilitation

MRPM is attacked because it might be used as a tool of collusion between dominant market retailers by tackling hurdles to price-fixing conspiracy namely establishment and enforcement.[29] The existence of MRPM could provide manufacturer as information tool to identify and punish cheating retailers by denying supplies and this policing role in downstream makes cartel stable.[30] However, the retailer should have significant market power as condition-precedent to secure MRPM from manufacturer.[31] The irony is that non-price vertical-restraints with outcome-equivalent for collusive behaviour of downstream as much as MPRM are regulated by rule of reason.[32] Moreover, the manufacturer has upper hand to overcome collusive-behaviour in downstream by setting price floor which bears less profit.[33] Even there exists high-profit caused by high-price because of MRPM and easy entry to retailing attracts new entrants to reduce price.

1.1.4 Foreclosing Competing Manufacturers

The existence of MRPM provides dominant manufacturer bargain chip with retailers by guaranteeing them lucrative profit margin in exchange for their refusal to distribute other incumbent manufacturers' (new entrants') goods.[34] This brings lack of substitute goods for consumer and causes welfare losses and disrupts Pareto-optimality. Citrus paribas, constrained consumption bundles entail no maximized utility for consumers. However, Thomas asserted that this scenario is not possible to

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[28] Yves Botteman & Kees J. Kuilwijk. (2010) 'Minimum) Resale Price Maintenance Under the New Guidelines: A Critique and A Suggestion'. *The Competition Policy International Antitrust Journal*, **1**, p.4.
[29] Lambert (supra note 27) p. 1944.
[30] Paldor (supra note 12) p.318.
[31] Id.p.327.
[32] Id.p.322.
[33] Bastiaan M. Overvest. (2012) 'A Note on Collusion and Resale Price Maintenance'. *EUR J Law Eco*, **34**:235-239, p.235.
[34] Herbert Hovenkamp (2005) *The Antitrust Enterprise: Principle and Execution*, Harvard University Press, Cambridge, p.162.

happen frequently as manufacturer might fail to convince retailers to refuse to distribute others' brand product.[35]

1.1.5 Softening Competition among Retailers

Strong downstream retailers may request MRPM to stave off competition from new entrants and retain customers. New-entrants lure consumers by having less price than the established retailers. Though cut-price is hard for entrants to lure consumers, still entrants could make profits by having greater efficiencies.[36]

1.1.6 Dampening System Competition through Interlocking

Bennett et al argued that in a situation of "double common agency" whereby the presence of both duopoly manufacturers and retailers in which both retailers distribute both manufacturers' product via networks of interlocking MRPM dampen competition.[37]

1.2 Pro-competitive Effect of MRPM

As single pro-competitive efficiency explanation does not offer an across-the-board justification for MRPM holistic sum of efficiency explanations must be sought.

1.2.1 Increasing inter-brand competition

MRPM avoids price-based competition among retailers and is criticised for not using cost-effective methods of selling.[38] Rather MRPM devises another instrument of competition that stimulates stiff competition among inter-brand manufacturers.[39]

1.2.2 Special Service & Free-Riding

Free-rider justification is the cornerstone of pro-competitive explanation. According to Telser, MRPM is justified by special service argument whereby manufacturer needs retailers providing customers with special service about the product that includes point-of-purchase sales promotion

[35] Lambert (supra note 27) p.1949-1950.
[36] Matthew Bennett, et al. (2011) 'Resale Price Maintenance: Explaining the Controversy, and Small Steps Towards a More Nuanced Policy'. *Fordham International Law Journal*, **33**(4):1278-1299, p. 1292.
[37] Id. p.1292-1293.
[38] Rimantas Daujotas (2011) 'Leegin case: Resale Price Maintenance vs. Consumer Welfare', p.7. Available at: http://ssrn.com/abstract=1866191 (Accessed 10 July 2016)
[39] Reindl (supra note 23) p.1319.

and information.[40] The customers need information which is costly and the manufacturer demands the retailers to disseminate information to customers. Paldor stated that provision of special services has the effect of raising price as service provider should cover cost of service and "stimulating additional demand" for manufacturer's product.[41] Paldor also added that the provision of the service is desirable and the cost of the service is covered by consumers' willingness to pay for the product. Service provider incurs the cost of training personnel, rooms for displaying-products, etc. and these costs are offset by increased demand for the product.

However, customers would get information from one retailer and purchase products from other retailer who doesn't bear the cost of providing special service. Non-service-provider retailer sells product due to information furnished to potential customers by service-provider retailer. Thus, non-service-provider retailer free rides at the expense of the service-provider-retailer. Paldor argued that service-provision brings positive "horizontal-externality" to free-riding-retailer by saving the cost of special-service-provision and shift it to under-price the product.[42] Therefore, Telser illustrated that MRPM is a means to avoid free-riding problem and achieve efficient-equilibrium when special-services provided. Paldor noted that the imposition of MRPM avoids under-price and retailers are compelled to compete on provision of service instead of price.[43] Consumers are endowed with choices ranging from low-price, low-service brands to high-price, high-service[44] and at times retailers providing presale product-service recoup return on investment from the services and sale made. It is agreed MRPM justification is applicable when the products are complex and sold with combined service as we will discuss latter.

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[40]Lester G. Telser. (1990) 'Why Should Manufacturers Want Fair Trade II'? *The Journal of Law and Economics*, **33**:409-417, p.409.
[41] Paldor (supra note 12) p.332.
[42] Id.p.332-333.
[43] Ibid.
[44]Tikoo & Mather (supra note 14) p.417-418.

1.2.3 Quality Certification for Reputation

Lao stated that "quality certification" is a variant of free-rider theory suggesting reputable retailer's holding of goods certifies their quality and free-riding happens when discounters who incurred no cost to develop-reputation sells to customers and eventually prevents retailers to invest in quality reputation.[45] Certification is signalling[46] the quality of the product to consumer. Imposing MRPM eliminates price competition and assured reputable retailer sufficient margin to recoup investment of service provision.[47]

1.2.4 Distributional Efficiency

Manufacturer chooses either vertically-integrated-distribution or buys market force to distribute its goods by making cost-benefit analysis of transaction cost.[48] Thomas asserted that manufacturer reaps benefits from retailer's special-distribution skill and lack of control over distribution service could be mitigated by MRPM.[49] He also stated MRPM provides leverage as "middle ground" where manufacturer secures benefits and avoids costs of buy and make choices.[50] Distributional-efficiency is critiqued because MRMP is hurdle to low-margin retailers to be innovative and transfer efficiency to consumers.[51]

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[45]Marina Lao. (2010) 'Resale Price Maintenance: The Internet Phenomenon and Free Rider Issues'. *The Antitrust Bulletin*, **55**(2):473-512, p.481.

[46] Howard Marvel & Stephen McCafferty. (1984) 'Resale Price Maintenance and Quality Certification'. *Rand Journal of Economics*,**15**(3):346-359, p.349.

[47] Paldor (supra note 12) p.341.

[48] Richard H. Coase. (1937) 'The Nature of the Firm'. *Economica New Seriess*, **4**(16):386-405, p.388.

[49] Lambert (supra note 27) p.1951-1952.

[50] Ibid.

[51]Warren S. Grimes (2009) 'Resale Price Maintenance: A Comparative Assessment', *Federal Trade Commission Panel on Resale Price Panel on Anticompetitive Effects*. Available at: https://www.ftc.gov/sites/default/files/documents/publicevents/resale_price_maintenance_under_sherman_act_and_federal_trade_commission_act/wgrimesppt0219.pdf.(Accessed 17 July 2016)

1.2.5 Contract Enforcement Mechanism Theory

Sometimes competitive-retailers may have an incentive to free-ride using manufacturer's reputation to provide a lower quality level than sought neither by manufacturer creating vertical externality nor anticipated by consumers.[52] Free-riding brings extra short-run profit to retailer and disincentive to provide desired service.[53] Therefore, manufacturer induces retailers to provide service via private enforcement mechanism that entitles manufacture monitoring and credible threat to terminate.[54] MRPM creates future-quasi-rents by devising incentives for retailers to pursue distributing of manufacturer's product.[55] It is assumed that potential future-rents lure the retailers not to engage in shirking MRPM.

1.2.6 The Outlets Theory

MRPM is called to function as substitute for directly limiting retailers number by getting rid of competition between retailers to achieve optimal density for retail network.[56] In such case, MRPM is employed as alternative to location clause.

1.2.7 Demand Risk Theory

Sometimes retailers suffer information asymmetry as to consumers' demand. When retailers are more risk averse, it is desirable to share risk between the parties. MRPM overcomes the uncertainty when demand turns out to be low.[57]

1.2.8 Easing Market Entry

MRPM enables market entry for new-products of firm by offering higher-retail-margin; retailers are induced to hold new-brands and provide sales effort that concomitantly encourages inter-brand-competition.[58]

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[52] Benjamin Klein & Kevin M. Murphy. (1988) 'Vertical Restraints as Contract Enforcement Mechanism'. *Journal of Law & Economics*, **31**:265-299, p.266.
[53] Ibid.
[54] Id.p.267.
[55] Id.p.268.
[56] J.R Gould & L.E Preston. (1965) 'Resale Price Maintenance and Retail Outlets'. *Economic*, **32**(127):302-312, p.304-306.
[57] Patrick Rey & Jean Tirole. (1986) 'The Logic of Vertical Restraints'. *The American Economic Review*, **76**(5):921-939, p.922.
[58] Tikoo & Mather (supra note 14) p.418.

In unilateral RPM by nonmonopolistic firm is permitted to refuse to deal with retailers which failed to comply with declared RPM whereas in bilateral RPM agreement firms prepare formal and enforceable RPM policies.[59] Vertical-restraints are substitutes for one another which means prohibition of MRPM induces firms to utilize exclusive territories, contractual arrangements, subsidizing retailers' effort and taking over markets from retailers which make competition authority sole deciding regulator as to distribution-methods.[60] Furthermore, substitution effects make firms substitute agency agreement for distributional agreement.[61]

The forgoing discussion reveals that when MRPM overall net social efficiency goals outweigh efficiency-loss, it should be subject to rule of reason otherwise subject to per se illegality.[62]

Each jurisdiction treats MRPM differently. "To supporters, it is "fair trade"; to opponents, "price fixing."[63] The following quote explains briefly

> Resale price maintenance (RPM) has had a history similar to that of a religious war, with the legal status shifting as the various sects have had more or less influence over the courts and the political arenas. Both the RPM and anti-RPM missionaries have overstated their cases. [64]

Section 2-MRPM in US and EU Competition Laws

Competition law is designed to achieve different objectives in different jurisdictions. Competition law comprises multiple and diversified goals. These include ensuring competitive process as goal and means, promote consumer welfare, enhance efficiency, ensure economic freedom,

[59] Id.p.421.

[60] Roger Van den Bergh. (2016) 'Vertical Restraints: The European Part of the Policy Failure'. *The Antitrust Bulletin*, **61**(1):167-185, p.175.

[61] European Commission (2010) '*Guidelines on Vertical Restraints, 2010/C 130/01*', at100. Available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:130:0001:0046:EN:PDF

[62] Paldor (supra note 12) p.351.

[63] Thomas Overstreet & Alan Fisher. (1985) 'Resale Price Maintenance and Distributional Efficiency: Some Lessons from the Past'. *Contemporary Economic Policy*, **3**(3):43-58, p.44.

[64] Id.p.43.

promote fairness, promote consumer choice, achieve market integration and promote competitiveness in international-market.[65]

Efficiency is economic term consisting allocative-efficiency which means resources allocation to most efficient use; productive-efficiency is producing by least cost way and dynamic-efficiency is rate of advent of new products or techniques.[66] This brings competition law to make trade-offs among irreconcilable efficiency goals pursued simultaneously that disrupts Pareto-efficiency. Efficiency and consumer welfare are separate concept and it is argued that competition-policy should accord priority to innovation and productive-efficiency which in the long-run protects consumer-welfare.[67] Welfare economics provides Kaldor-Hicks efficiency that allows existence of both winners and losers, however, demands the winners gain more than the loser lose and out of the surplus the winners pay potential compensation. Kaldor-Hicks efficiency concerns aggregate (total-welfare) rather than individual-welfare. Total welfare implies the total sum of producer and consumer surplus maximization. Total-welfare is concerned on how the pie (total surplus) is enlarged due to productive (dynamic-efficiency).

2.1 MRPM in US Antitrust Law

Antitrust policy emerged as compromise between irreconcilable laissez-faire and interventionist-ideologies.[68]Whether total-surplus, consumer-surplus or "weighted average of producer plus consumer-surplus" should

[65] International Competition Network (2007) 'Report on the Objectives of Unilateral Conduct Laws, Assessment of Dominance/Substantial Market Power, and State-Created Monopolies', p.4-12. Available at: http://www.internationalcompetitionnetwork.org/uploads/library/doc353.pdf.(Accessed 6 May 2016)

[66] Ibid.

[67] Joseph F. Brodley. (1987) 'The Economic Goals of Antitrust: Efficiency, Consumer Welfare, and Technological Progress'. N.Y.U.L.Rev, **62**:1020-1053, p.1021.

[68] John Lopatka & William Page ''Obvious' Consumer Harm in Antitrust Policy: The Chicago School, the Post-Chicago School and the Courts': Cited in Antonio Cucinotta, Roberto Pardolesi & Roger Van den Bergh(eds.) (2002) *Post-Chicago Developments in Antitrust Law- New Horizons in Law and Economics*, MPG Books Ltd, Bodmin, Cornwall, ISBN 1843760010, p.129.

be maximized is fierce on-going debate in US.[69] US values the importance of innovation to competition policy because innovation leads dynamic-efficiency.[70] Chicago School has influenced US Supreme-Court to embrace economic goals (total welfare). The US Supreme-Court rarely takes consumers' interest as paramount concern in competition-law.[71] Even Sherman's letters depicted that his concern was protecting interest of business than consumers'-interest.[72]

Sherman Act was enacted in 1890. Sherman Act-Section-1 was the ground on which interpretation was made to prohibit vertical-restraints reads:

> 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 declared to be illegal. Every person who shall make any contract or engage in any combination or conspiracy hereby declared to be illegal...[73]

Troesken noted competing rationales for origin of Sherman Act are analysed by three schools of thought. Traditional interpretation argues the Act was enacted to promote consumers' welfare and to restrain market power whereas revisionist interpretation opines small businesses were strong lobbyists for antitrust to weaken efficient trusts and finally the hybrid interpretation suggests small business backed up antitrust to counterbalance strong trusts using vertical restraints, etc.[74]

When Sherman introduced antitrust bill, small businesses and retailers wrote letters expressing discontent on vertical-restraints.[75] Many types of trusts employed vertical-restraint to shape retailers' behaviour in the business-arena. The pressure stemmed from retailers, rivals and small

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[69] Dennis Carlton. (2007) 'Does Antitrust Need to be Modernized'? *Journal of Economic Perspectives*, **21**(3):155-176, p.157.
[70] Rudolph Peritz 'Dynamic efficiency and US antitrust policy': Cited in (supra note 68) p.108-109.
[71] Lopatka & Page (supra note 68) p.131.
[72] Werner Troesken. (2002) The Letters of John Sherman and the Origins of Antitrust. *The Review of Austrian Economics*, **15**(4):275-295, p.275.
[73] *The Sherman Antitrust Act*, 1890.
[74] Troesken (supra note 72) p.275.
[75] Id.p.285.

business firms prompted trusts to integrate-vertically.[76] However, Sherman was neither friend of consumer or small-firms discontented by vertical-restraints nor adhered vertical-restraints in the proposal.[77]

2. 2 MRPM in US Case Law

The Supreme-Court in Dr. Miles decisions decided that manufacturer's setting minimum prices at which retailers resell the product was illegal that falls under the ambit of common law and Sherman Act Section-1.[78] Dr. Miles Company was active manufacturer and seller of proprietary medicines which were prepared in secret and widely traded in US. The Company channelled its product via wholesaler by fixed-price for the wholesaler and retailers.[79] The Company concluded written agreement that compelled the retailer-agent not to sell the medicines at any price quoted and not to sell for unaccredited retailers by the Company. Dr. Miles sued John D. Parks & Co. drug wholesaler which refused to enter into consignment agreement but sold Dr. Miles' medicines securing fraudulently from the rest accredited consignees and agents. The basis of argument was that the manufacturer shouldn't impose MRPM because "the right of alienation is one of the essential incidents of a right of general property in movables and restraints upon alienation have been generally regarded as obnoxious."[80] Thus the Court was concerned about the property rights of retailers' and freedom of distribution not the analysis of economic justification of MRPM in antitrust law ambit.

This laid the foundation for per se rule under which agreements are prohibited according to Sherman Act Section-1 without considering the effect.[81] Though US depicted progressive tolerance for vertical-restraints,

[76] Id.p.286.
[77] Id.p.291-292.
[78] Barbara Bruckmann (2007) 'Revisiting Dr. Miles: Reinstating a Modern Rule of Reason for Vertical Minimum Resale Price Agreements', *The Antitrust Source*, p.1. Available at: www.antitrustsource.com (Accessed July 2016)
[79] *Dr. Miles Medical Company v. John D. Park & Sons Company, Certiorari to the Circuit Court of Appeals for the Sixth Circuit*, No. 72. p.374, 1911.
[80] Id.p.404.
[81] Bruckmann (supra note 78).

it has imposed per se illegal rule against vertical-restraints until 1970s.[82] In US vertical-restraints are categorized into two namely price and non-price restraints.[83] Price restraints are either MRPM or maximum RPM which firm forces retailers to comply with whereas non-price vertical-restraints contain blanket class of all other restraints.

The Chicago School has adhered to per se legality based on efficiency justifications. Long struggle between schools of thought help US has solid tradition of competition law based on economic-analysis.[84] When time went by, US antitrust case subordinated non-economic goals to the fulfilment of economic efficiency.[85] In Sylvania ruling, the Supreme Court rejected per se rule in non-price-vertical restraints and brings rule of reason. The verdict reads as follow:

> There are certain 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. Similarly, the facts of this case do not present a situation justifying a per se rule. Accordingly, the per se rule stated in Schwinn is overruled, and the location restriction used by respondent should be judged under the traditional rule of reason standard.[86]

In similar vein, the Supreme Court passed the verdict avoiding per se illegality of price constraint against namely maximum RPM and MRPM and subject to rule of reason.

The Supreme Court in *State Oil v. Khan Case* overruled per se illegality of maximum RPM and subject it under rule of reason. In this case, operators of gas station concluded agreement with oil company that fixed

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[82] Sandra Marco Colin (2010) *Vertical Agreements and Competition Law: A Comparative Study of the EU and US Regimes*, Hart Publishing Ltd, Oxford, ISBN 978-1-84113-871-8, p.15.

[83]Yossi Spiegel & Yaron Yehezkel (2000) 'Price and non-price restraints when retailers are vertically Differentiated', p.2. Available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=236024 (Accessed 20 May 2016)

[84] Colin (supra note 82) p.47.

[85] Id.p.49.

[86]*Continental T.V. Inc. v. GTE Sylvania, Inc. 433 U.S*. 36, 1977.

maximum gasoline price and retailers are forced not to exceed the suggested retail price.[87]

After almost a century of Dr. Miles, US Supreme Court overruled the per se prohibition of MRPM in Leegin case.[88] The Court seemed to follow Hayek's path. Hayek stresses that competition serves as "discovery procedure" that emphasizes the role of the case-by-case analysis favouring rule of reason.[89]

Leegin adhered the policy of refusing to sell to retailers which fall to observe the suggested prices. PSKS sued Leegin claiming that it violated antitrust laws by forcing to enter vertical agreement to set MRPM. PSKS was selling Leegin's product prices as low as 20% below the minimum-price ordered by Leegin and refused to halt this practice to get discount.

The Court tried to distinguish between restraints with anticompetitive effect that are harmful to consumer and with competitive effect to the best interest of consumer. The Court stipulated that rule of reason demands factfinder to weigh "all of the circumstances."[90] Both the Court and each parties back up the debate from economics perspective and employ extensive economic-literature. The Court argued that rule of reason's case-by-case decision entertains common law statute and replaces per se illegality with rule of reason. The Court, however, cautioned that "it can't be stated with any degree of confidence that MRPM 'always or almost always tends to restrict competition and decrease output'."[91] In dissenting opinion, Breyer articulated that "…antitrust law cannot, and should not, precisely replicate economists'…views."[92] Hence rule of reason is applicable when the total welfare effect outweighs the loss by assessing the context. Price-competition is not the only goals of competition law but

[87] *State Oil Co. v. Barkat U. Khan and Khan & Associates Inc.118* S. Ct. 275, 1997.
[88] *Leegin Creative Leather Products, Inc. v. PSKS, Inc., 551* U.S. 877, 2007.
[89] Friedrich Hayek (1973) *Law, Legislation, and Liberty: A New Statement of the Liberal Principles of Justice and Political Economy*, T.J. International Ltd. Cornwall, ISBN 0-415-09868-8, p.67.
[90] Leegin (supra note 88).
[91] Ibid.
[92] Ibid.

also "quality-or-variety-increase-investment" competition.[93] Furthermore, US Supreme Court realizes the similar effect of both price and non-price effect of restraints and progressively lifted per se illegality and replaces with rule of reason.

2.3 MRPM in EU Laws

Achieving market-integration is the goal of competition-law in EU. European-Commission competition policy is charged with the task of being a means to the mission accomplishing of the internal market via abolition of trade barriers.[94] The legal basis for the prohibition of vertical-restraints in EU is Article-101. It prohibits those acts which hamper internal market and stipulates

> The following shall be incompatible with internal market: all agreements between undertaking…decisions by associations of undertakings and concerted practice which may affect trade…have as their object or effect the prevention, restriction or distortion of competition within the internal market, in particular.[95]

The more elaborated explicit discussion appeared in the landmark case of *Grundig/Consten* which laid the foundation that Article-101 comprises both horizontal and vertical-agreements.[96]

The European-Commission has introduced block exemption to clear confusion regarding the permitted and prohibited agreements. In regulation 330/2010, EU introduces quasi per se prohibition of vertical MRPM.[97] The prohibition of RPM extends to both direct agreements on fixed (MRPs) or agreements serving the purpose of RPM via indirect means such as fixed distribution margins, maximum discount levels, rebate dependent on the observance given price level or termination of deliveries due to low price level.[98] The Commission stipulates that

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[93]Richard Markovits (2014) *Economics and the Interpretation and Application of U.S and E.U. Antitrust Law: Volume II Economics-Based Legal Analyses of Mergers, Vertical Practices, and Joint Ventures*, Springer, New York, p.VIII.

[94] ICN (supra note 65) p.19.

[95] *Consolidated Versions of the Treaty on European Union and the Treaty on the Functioning of the European Union, 2008/C115/01*.

[96] Opinion of Mr. Advocate-General Roemer Delivered, 1966 on Joined Cases 56 and 58/64, at 299 in *Consten and Grundig v. Commission*, E.C.R.

[97] Bergh (supra note 60) p.171.

[98] Ibid.

banning of MRPM is justified because of its anticompetitive effects: encourages collusion among sellers or buyers, stifling competition at different levels of trade, results in exorbitant price, foreclosure of rival firms, softening dynamism and innovation at distributional level.[99] However, European competition authority realizes that supplier-driven MRPM may lead to efficiency in case of experience and credence goods by preventing free-riding and lying the burden of proof on firm to ascertain distributional-efficiencies.[100]

Many seminal articles cogently argued that vertical-restraints are employed as devices to tackle externalities, solve principal-agent problems and reduction of transaction-costs.[101] The existence of divergence of literature on 'vertical restraints effect'[102] compels economists to plead in favour of an effect-based approach focusing on efficiency benefits and potential anticompetitive effects of vertical restraints rather than purely form-based legalistic approach.[103] Thus "efficiency as a legal concern" is used to justify public policy decisions.[104] Taking efficiency, EU Commission has reiterated that "economics-based approach" is to be preferred to strictly legalistic-approach of decision making in area of vertical restraints.[105] Similarly, the European Court of Justice had adhered to more economically inspired reasoning.[106] Professor Roger stipulated that vertical-restraints may have both beneficial and harmful effects and goes on:

> *If vertical restraints were used mainly to improve distribution efficiency, rather than to support collusion or erect entry barriers, they could be held simply legal.*

[99] European Commission (supra note 61) at.100.
[100] Id.225.
[101] Rey & Tirole (supra note 57) p.921.
[102] Patrick Rey & T. Verge. (2010) 'Resale Price Maintenance and Interlocking Relationships'. *J. IND.ECON*, **58**, p.828.
[103] Bergh (supra note 60) p.173.
[104] Andrea Renda, (2011) '*Law and Economics in the RIA World'*. PhD Dissertation, Erasmus University Rotterdam, p.10.
[105] Cucinotta, Pardolesi & Bergh (supra note 68) p.VIII.
[106] Roger Van den Bergh 'The Difficult Reception of Economic Analysis in European Competition Law': Cited in (supra note 68) p.34.

> The difficult task of competition policy is to distinguish between both hypotheses and to enable a trade off if vertical restraints at the same time produce anticompetitive effects and achieve efficiencies. In spite of these difficulties, the following two lessons may be derived from the economic analysis. First, the economic consequences of vertical restraints and not their legal form should be decisive in judging their conformity with the competition rules. Second, economic analysis does not provide a justification for the different treatment of different types of vertical restraints, since they are substitutes for each other.[107]

Professor Roger states that EU competition-law guarantees no full efficiency-analysis of vertical-restraints but U.S. rule of reason does.[108] Even though EU has exerted to instil "economic based approach", Professor Roger suspects that it would be premature, however, to characterize the new rules as a complete victory of economics and effects based law making. He concludes "there is no perfect harmony between competition economics and competition law."[109] As long as the aim of competition-law which is "single market integration" is highly prized, it poses threat to advent rule of reason. This means internal market objectives shadow productive and allocative efficiency in European competition-law.[110] Even the opinion of Advocate General in T-Mobile case, it is well articulated that Article-101 is designed to "protect not only the immediate interest of individual competitors or consumers but also to protect the structure of the market and thus competition as such (as an institution)."[111]

The preceding discussion shows US Supreme-Court has progressively changed hardcore (form-based, per se illegality) to effect-based (soft, rule of reason). Nevertheless, 'efficiency defence' in EU is severely limited.[112] Legal certainty which is achieved by "simple" rules rather than complete economic-analysis are responsible for not flourishing effect-based

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[107] Id.p.38.
[108] Bergh (supra note 60) p.173.
[109] Ibid.
[110] Bergh (supra note 106) p.42.
[111] Opinion of Advocate General Kokott, 2009, Case C-8/08, at 58 in T-*Mobile Netherlands Bv et al v. Raad Nederlandse Mededingingsautoriteit*.
[112] Bergh (supra note 106) p.43.

analysis of rules.[113] For the abolition of per se illegality and to the advent of the rule of reason, by Supreme Court, Chicago School has supplied effect-based analysis by using economics tools.

Section 3- Per Se Illegality and Rule of Reason

Chicago School helped flourished price-theory as a powerful tool to examine competition-law and non-price forms of competition as a gap-filling or subsidiary-role.[114] Unlike Harvard School which accepts multitude of goals, Chicago School advanced productive and allocative efficiency as the only objectives to be a guide in interpreting and applying competition-law.[115]

The "pursuit of economic efficiency" is the goal of antitrust policy for Chicagoans in which efficiency-enhancing (gain) dealing is the heart of the antitrust-policy-goal.[116] The Chicago School strong influence on US antitrust-policy emerged as of 1970s and reached its climax using price-theory.[117] However, European Competition-law is unflinched from integration-goal and pursuit of economic efficiency has been sidelined and yet European-Commission has been tempted by economic efficiency-gains as illustrated in *Wanado*.[118]

3.1 Per Se Rule

Per se rule is always anticompetitive and grants automatic violation.[119] This is hard-core violation that needs no defenses (justifications) are allowed when the fact existing depicts violation as observed in US

[113] Id.p.56.

[114] Roger van den Bergh & Peter Camesasca (2006) *European Competition Law and Economics: A Comparative Perspective,* Sweet & Maxwell, New York ISBN:9780421965805, p.79.
[115]Ibid.
[116] Id.p.84.
[117] Ibid.
[118]Id.p.85
[119] Bryce J. Jones & James R. Turner. (2010) 'The Fall of the Per Se Vertical Price Fixing Rule'. *Journal of Legal, Ethical and Regulatory Issues*, **13**(2) p.83-84.

Supreme Court.[120] There is no need to adduce evidence that practice is anticompetitive as assumption is taken.[121] Per se rule is comparatively easy for antitrust authorities and plaintiffs when the facts exist.[122] Per se rule prohibited restraints such as horizontal price fixing, tying, vertical non-price and price restraints and it was condemned that per se approach was over-inclusive, overly formalistic and avoids pro-competitive gains.[123] The Court applied per se analysis if the conduct is "manifestly anticompetitive" or the practice demonstrates "pernicious effect on competition" and devoid of any redeeming value.[124] Per se rule has the advantage of lower regulation-costs, reduce rent-seeking and minimize knowledge problems.[125]

3.2 Rule of Reason

This is a shift from rules based on forms (formalistic-approach) to rules based on economic-efficiency effect (effect-based-approach).[126] When the net economic efficiency outweighs anticompetitive effect and is demonstrated with experts it is called rule of reason.[127] To prove net effect in rule of reason is painstaking task and difficult to win and makes courts sceptical of rule of reason.[128] Hovenkamp noted "…the rule of reason created one of the most costly procedures in antitrust practice."[129] Even with this risk, the actual (potential) economic effects of challenged practice under the context is analysed. Rule of reason engages in case-by-

[120] Ibid.
[121] Ibid.
[122] Ibid.
[123] Alison Jones. (2010) 'The Journey toward an Effects-Based Approach under Article 101 TFEU-The Case of Hardcore Restraints'. *The Antitrust Bulletin*, **55**(4):783-818, p.784.
[124] Tye Darland. (1989) 'Antitrust Law- Vertical Price Restraints: Per se Illegality or Rule of Reason'? Business Electronics Corp. v. Sharp Electronics Corp, Comment. *The Journal of Corporation Law*, **14**:495-513, p.496.
[125] Arndt Christiansen & Wolfgang Kerber, 2006. Competition Policy with Optimally Differentiated Rules Instead of "Per Se Rules Vs Rule of Reason". *Journal of Competition Law and Economics*, **2**(2):215-244, p.216.
[126] Jones (supra note 123) p.784.
[127] Jones &Turner (supra note 119) p.84.
[128] Ibid.
[129] Hovenkamp (supra note 34) p.105.

case analysis to examine whether the complained conduct violates given competition-law by granting flexibility to court.[130] Rule of reason is not automatically legal but close to legal.[131]

While discussing rule of reason Bork articulates that "consumer welfare'' is the thrust of antitrust law. Bork put consumer welfare "whole task of antitrust can be summed up as the effort to improve allocative efficiency without impairing efficiency so greatly as to produce either no gain or a net loss in consumer welfare."[132] Bork noted that antitrust shouldn't have both equity and income distribution concern as "shift in income distribution does not lessen total wealth."[133] "Consumer'' is broadly interpreted consisting of business buyers, sellers, and individual consumers.[134]

Posner criticised rule of reason saying "it is little more than a euphemism for nonliability."[135] Even Peter went too far and proposed for removal of the rule of reason arguing free market has comparative-advantage over judicial-evaluation.[136] However, taking efficiency, Bork argued, in favour of rule of reason, that all vertical restraints "should be completely lawful."[137] The rule of reason is allowed to offer opportunity "for novel business practices to come under close and careful scrutiny so that their true economic effect might be evaluated."[138] This means accepted overriding goal of competition law should be economic efficiency (aggregate economic-welfare) which serves as a value-free goal that saves judges from imposing personal thoughts as regard to fair business

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[130] Darland (supra note 124) p.496.
[131] Jones &Turner (supra note 119) p.84.
[132] Robert Bork (1978) *The Antitrust Paradox*, Basic Books Inc, New York: Cited in Jones & Turner, p.97.
[133] Id.p.97.
[134] Ibid.p.97.
[135] Richard A. Posner. (1977) 'The Rule of Reason and the Economic Approach: Reflection on the *Sylvania* Decision'. *The University of Chicago Law Review*, **45**(1):1-20, p.14.
[136] Peter Nealis. (2000) 'Per Se Legality: A New Standard in Antitrust Adjudication Under the Rule of Reason'. *Ohio State Law Journal*, **61**:347-398, p.349.
[137] Jones &Turner (supra note 132) p.98.
[138] Nealis (supra note 136) p.348.

practice.[139] This economic-efficiency is "aggregate economic welfare" that sums consumer welfare and stockholder profits.[140]

In order to bless rule of reason, courts examine three evaluations: a) the degree of competitive harm from defendants' practice; b) existence of legitimate and useful activities of the participants; c) whether legitimate purpose is achieved by another less restrictive means or not. [141] Both positive and negative effects of the practice are examined.

Rule of reason is rebuttable presumption which is utilized to analyse RPM.[142] However, courts in applying the rule of reason are prone to decision-error costs. Therefore, it is better to minimize the sum of welfare costs resulted from decision errors of type I ("false positives") and type II ("false negatives") and the costs of applying of rules.[143] Type I error occurs when the practice with negative welfare effect is mistakenly allowed whereas type II error happens when practice with positive welfare effect is mistakenly prohibited.[144]

Section 4- Economic Analysis of Minimum Resale Price Maintenance Prohibition in Ethiopian Competition Law

4.1 Economic Efficiency Defense in Previous Legislations

The approaches as to the relevance and the content of competition-policy and law are varied. The argument includes weak institutional capacity of developing countries may not be conducive environment for intensive competition and invites strong-state to handle comprehensive and intensive competition policy.[145] It is suggested that developing country competition-law must promote long-term growth of productivity and as unrestricted competition policy emphasized on efficiency is suitable to developed economies.[146] One-size-fits-all-approach doesn't seem to hold

[139] Id.p.351-352.
[140] Ibid.
[141] Id.p.359.
[142] Pamela Jones Harbour & Laurel A. Price. (2010) 'RMP and the Rule of Reason: Ready or not, here we come'? *The Antitrust Bulletin*, **55**(1):225-244, p.225.
[143] Christiansen & Kerber (supra note 125) p.216.
[144] Id.p.225.
[145] Kibre (supra note5) p.15.
[146] Id.p.16.

as Colombia which is small economy accords weight to economic-efficiency.[147] Ethiopia is not an exception to this and enacted legislations which allow anticompetitive practices as long as economic-efficiency is offset.

So far Ethiopia has enacted three competition proclamations. Because of liberalization measures as groundwork for the WTO accession, Ethiopia enacted TPP in 2003. Ethiopia introduced TPP that emphasized, at the preamble, the desirability "to establish a system that is conducive to the promotion of competitive environment, by regulating anti-competitive-practices in order to maximize economic-efficiency and social welfare."[148] Article-3 reads objective "to secure fair competition process" by preventing and eliminating anticompetitive practice.

TPP doesn't explicitly deal with vertical-restraints rather sets general prohibition under Article 6(1) as follows: no person is allowed to "enter into any written or oral agreement that restricts, limits, impedes or in any other way harms free competition…distribution…" This is similar to Sherman Act Section one whose interpretation was made to prohibit vertical-restraints even in the absence of the explicit words of vertical restraints. It offers hints about vertical restraints as the word distribution implies. Hailegebriel argued that despite no complete verbal similarity corresponding Article-6(1) and EC-Treaty Article-81(1) the former is influenced by the latter.[149]

Notwithstanding Article-6(1) the Ministry may bless entry into any competition harming agreement "after making the necessary studies, and ensuring that advantages of the agreement to the Nation is greater than the disadvantages."[150] The authorization of this agreement may be cancelled *"in the event that the advantages to the nation are no longer greater than the advantages*" emphasis added.[151] Therefore the Ministry periodically

[147] R. Shyam Khemani (2002) 'Application of Competitive Law: Exemptions and Exceptions', *United Nations Conference on Trade and Development*. New York, p.8.
[148] TPP (supra note 2)
[149] Hailegabriel (supra note 7) p.274.
[150] TPP (supra note 2) Article7.
[151] Id.Article 9.

assesses advantages and disadvantages of authorized agreement. It is clear that economic-efficiency (total welfare) is accorded priority in this legislation. It is argued that recognition of economic analysis of anticompetitive practices with ex-ante authorisation exists under Article-7 as the phrase "*ensuring that advantages of the agreement to the Nation is greater than the disadvantages*" is apparently broad enough to be interpreted as *economic or non-economic analysis* of factors.[152]

Legal and structural limitations as well as exclusion of consumer protection provisions of this proclamation led to the enactment of TPCPP. This proclamation under Article 3 sets the objective of "protecting consumers' rights and benefits" and "accelerating economic development."[153] Article 9(3) allows abuse of market dominance when it is "achieving efficiency and competitiveness."[154] Moreover, Article-10 stated that the Council of Minister may enact regulation to exempt trade activities of abuse of market dominance when it finds such activities are necessary for facilitating economic development.

Article 13(1(b)) absolutely prohibits any "agreement between business persons in a vertical relationship that has an object or effect of setting minimum retail price." TPCPP explicitly recognizes prohibition of MRPM, unlike its predecessor. The proclamation doesn't explicitly mention the prohibition of non-price vertical-restraints.

Article 13(1(b)) resembles its European counterpart and witnesses European Competition Law Article 101 mark. Reindl pointed that RPM as "restriction by object" is characterised as a "hardcore" violation.[155] The following explains;

> The difference between "restriction by object" and "restriction by effect" does not reflect two entirely separate analytical standards. It would be incorrect to assume that article 101 TFEU has only two diametrically opposed analytical routes: one that is inflexible and never requires any scrutiny of the circumstances in which an agreement occurs, and another that always requires a full-blown analysis in which

[152] Hailegabriel (supra note 7) p.282.
[153] TPCPP (supra note 4)
[154] Id.Article 9(3).
[155] Reindl (supra note 23) p.1303.

> an elaborate examination of relevant markets, market power, and anticompetitive effects is required-a standard that plaintiffs invariably are unable to provide. Rather, these two approaches represent two poles at each end of a spectrum that cover more nuanced analytical approaches in between.[156]

Some practices may have restriction of competition as "object" for instance, price fixing, limiting output and restriction on sales whereas other agreements don't have restriction of competition as their object which requires identification of latent restrictive effects of agreement that demands examination of economic analysis before prohibition.[157]

Article 14 allows MRPM and stated that if the business person prove technological or efficiency or other pro-competitive gains of the agreement outweigh detriments of the prohibited acts, he is relieved from being accused and his anticompetitive practices are blessed.

The discussion made here demonstrated that previous legislations constantly held the rule of reason as dear value. There was big leeway left for economic analysis in previous legislations implicitly and explicitly.

There was no automatic prohibition of anticompetitive practice rather these practices were blessed when there are efficiency defenses. Anticompetitive practices were not condemned without inquiry into the actual effects on competition. This is rule of reason in which the potential and actual competitive effects of a challenged practice under the market is analysed contextually. Economic efficiency was the priority. And this economic efficiency justification is even adopted in harsh horizontal agreement, abuse of market dominance and merger cases. To pass the test the total-welfare gain must exceed the total-loss.

4.2 Economic Efficiency Defense in Current Proclamation

The declared policy objectives of competition law are set out in preamble and Article 3 of current TCCP.[158] Hence goal of competition law is not a single goal rather multiple goals are recognized. When competition law objectives and different policies (economic objectives) in other economy sectors become at loggerheads, the latter takes precedence over the former

[156] Id.p.1300.
[157] Hailegabriel (supra note 7) p.283 footnote 41.
[158] TCCP (supra note 8)

and exempted from the whole application of TCCP according to Article 4(2) of TCCP.

Words "exemption" and "exception" are appeared frequently in competition law policy. "Exemption" is "excused or free from some obligation to which others are subject" whereas "exception" is exclusion "from or not conforming to a general class, principle, rule, etc."[159] Exemptions are broader in scope whereas exceptions are narrow in focus and examined on a case-by-case basis applying the rule of reason approach.[160] "Best practice" dictates that competition law should be "general law of general application" indiscriminately applied to "all sectors and all economic agents" in economy take part in commercial activities both private and public.[161]

Article 5 prohibits abuse of market dominance. However, abuse of market dominance is exceptionally allowed according to Article 5(3) when the existence of "justifiable economic reasons" are proved. The exception under Article 5(3) of TCCP is narrower than TPCPP which contained broad phrase "legitimate business purposes" under Article 9. Naked horizontal agreement and vertical restraints (except MRPM) are blessed exceptionally as long as efficiency defense exists.[162] Article 11(2) overrides exceptionally and allows merger as long as merger results in efficiency or other pro-competitive gain that outweigh the significant adverse effect of merger.

To sum up, it is clear that TCCP emphasizes and adopts economic efficiency justifications exceptionally in many anticompetitive practices. Furthermore, it dropped per se or absolute prohibition. However, TCCP is hostile to MRPM and denies economic efficiency defenses in exceptional circumstances, unlike the previous legislation which allowed exceptional economic efficiency defense for MRPM. The current legislation swerved

[159] Khemani (supra note 147) p.1.
[160] Id.p.2.
[161] Id.p.5.
[162] TCCP (supra note 8) Article 7(1(a) & 2(a))

out of economic efficiency defense path which was possible in TPCPP. Competition law has evolved from legalistic formal approach to effect-based approach that focuses on the impact of MRPM on economic efficiency. Non-price vertical-restraints which may serve the same economic goal are not explicitly prohibited and any vertical restraint which produces efficiency is allowed. Apart from MRPM, there is perfect harmony between competition economics and TCCP. The attitude held by stakeholders of competition law and policy towards vertical restraints "varies significantly from one period to another"[163] holds water to Ethiopian context.

4.3 Economic Analysis of MRPM

MRPM needs at least three parties to the relationship for analysing the full effect of MRPM on economic efficiency defense; namely manufacturing firm which manufactures and at least two retailers which distribute manufacturer's product.

TCCP under Article 7(2(b)) states that vertical relationship shall be prohibited when setting of minimum resale price occurs and no exception is allowed regardless of efficiency justification. In a similar vein, any person who transgressed Article 7(2(b)) shall be punished with a fine of 10% of total annual turnover. It is this Article's view that economic efficiency is best served when MRPM is judged according to a rule of reason.

4.3.1 Total Welfare-Utility Maximizing

The prohibition of MRPM is justified by price hikes. However, Reindl submitted that price test is outright wrong hence, MRPM's effect on output should be taken as a proxy instead of prices.[164] MRPM effect on price increase is ambiguous. Assume MRPM is imposed and the price for goods g manufactured by firm shows increasing which means current price is greater than initial price(pc>pi). In the midst of this, when output increases even though price increase which means current quantity is

[163] Patrick Rey & Thibaud Verge. (2010) 'Resale Price Maintenance and Interlocking Relationship'. *The Journal of Industrial Economics*, **8**(4):928-961, p.928.
[164] Reindl (supra note 23) p.1319-1320.

greater than initial quantity (qc>qi) this illustrates the consumer value the enhanced services provided and willing to buy goods for the greater price for the exchange of rendered services. In such case, the marginal utility of the consumer derives is the difference between marginal utility of goods g less (pc-pi). When the total utility from increased service quality rendered is greater than the price imposed, MRPM will not lead a decrease in total consumer welfare.

The relation between price increase and output is affected by the elasticity of goods manufactured by firm which takes either of pcqc>piqi, pcqc=piqi or pcqc<piqi.[165] In such case, the ratio of marginal consumers to infra-marginal consumers are crucial to analyse the effect of MRPM. If marginal consumers are willing and able to pay more for special service provision but infra-marginal consumers would opt lower special service provision, manufacturer seeks to increase special service.

Consumer surplus measures consumer welfare.[166] However, there is "misunderstanding" between consumer surplus and consumer welfare which is called "Chicago Trap" and the proxies for welfare are allocative efficiency, economic welfare, and wealth.[167] Bork defined "consumer welfare" as total welfare but others misunderstood this as consumer surplus.[168]

Often, welfare analysis is static that concerns only current welfare and ignores the future welfare effect.[169] Literarily, welfare is reduced to "price advantage" whereby "benefits" is interpreted as "price reduction" and "harm" means price increase.[170] This is a neoclassical economy concept that measures consumer surplus in price terms and concerns on distributive justice aspect that shifts wealth in favour of consumers rather than producing total wealth.

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[165] Cemre & Semih (supra note 9) p.13.

[166] Victoria Daskalova. (2015) 'Consumer Welfare in EU Competition Law: What Is It (Not) About'? *The Competition Law Review*, **11**(1):133-162, p.137.

[167] Id.p.143.

[168] Robert Lande. (1999) 'Proving the Obvious: The Antitrust Laws Were Passed to Protect Consumers (Not Just to Increase Efficiency)'. *Hastings L. J*, **50**:959-968, p.961.

[169] Daskalova (supra note 166) p.137.

[170] Ibid.

The consumer is end user (final consumer) in TCCP. TCCP Article 3(2) price effect becomes as one of the objectives of competition law. This implies retailers shouldn't be prohibited from competing on price to get reduced price for consumers through MRPM. MRPM avoids myopic price competition objective and rather pushes retailers to compete on special services (sales effort) to attract customers. TCCP objective under Article 3(2) seems akin to EU's 1997 "Green Paper on Vertical Restraints" definition which states that "effective competition is the best guarantee for consumers to be able to buy good quality products at the lowest possible prices."[171] However, consumer welfare consists more than price such as quality, safety, choice, and innovation.[172] The total welfare effect should be guiding principle rather than narrowed consumer welfare to evaluate MRPM effect. Increasing the pie (total welfare) should be the goal of competition law not distributing the pie (distribution justice) which should be the task of other laws.

4.3.2 MRPM and Transaction Cost Approach

Distribution has costs and the manufacturer has choices of either using firm solution by establishing its own distribution channels or market solutions by contracting with independent retailers to distribute its goods.[173] When the manufacturer opts for a market solution (retailers' distribution channel), it creates appropriable quasi-rents which lead to lock-in effect as a result of specific investments and this makes reign opportunistic behaviour.[174] It is obvious that in long term contract sunk

[171] EU Commission (1997) 'Green Paper on Vertical Restraints in EC Competition Policy', p. 17. Available at: http://www.ab.gov.tr/files/ardb/evt/1_avrupa_birligi/1_6_raporlar/1_2_green_papers/com1997_green_paper_on_vertical_restraints_ec_competition_policy.pdf. (Accessed 9 July 2016.)

[172] Case C-209/10 *Post Danmark A/S v Konkurrencerådet* [2012] (electronic Reports of Cases), at 22.

[173] Oliver E. Williamson. (1974) 'The Economics of Antitrust: Transaction Cost Considerations'. *Pennsylvania Law Review,* **122**:1439-1496, p.1450.

[174] Benjamin Klein, Robert Crawford & Armen Alchian. (1978) 'Vertical Integration, Appropriable Rents, and the Competitive Contracting Process'. *Journal of Law and Economics*, **21**(2):297-326, p.298.

cost is huge and parties won't make investment unless they devise a mechanism to avoid hold-up problem.

MRPM could be employed as a tool to tackle the problem of shirking contractual duties among the contractual parties. RPM plays "the additional role of protecting rents to retailers"[175] and eliminate ex-post form of opportunistic rent shifting. For example, retailer A invests in special service-provision of manufacturer's product. Training of personnel, building of shops and other costs are sunk costs retailer A invested and he is locked-in. On the contrary, Retailer C, doesn't invest rather collects benefits via free-riding by saving the cost of special service provision and shift this cost to under-price special service providing retailer's goods. Retailer C acts opportunistically. This is what we call "horizontal externality". Retailer A seeks commitment device to claim the residual value of his investment. MRPM prohibits under-pricing by Retailer C and forces him to compete on sales effort.

Retailer A would be encouraged to invest and reap the benefit of his investment as long as he is protected from opportunistic behaviour. Hence, MRPM guards Retailer A's quasi-rents against erosion by Retailer C price competition and forces to compete on sales effort competition.[176] Retailer A calculates the degree of appropriability of quasi-rents when he invests and Retailer C sticks to opportunistic situations to hold-up when quasi-rents generated. MRPM avoids under-provision of special service due to hold-up problem.

4.3.3 MRPM and Free-Riding

It is argued that curbing free-riding produces efficient distribution by retailers. When retailers' margins increase the price goes up and drop in product sales follows. Hence, the intention of imposing MRPM by manufacturer is to protect price increase and drop of sales.

Free-riding is a negative externality created when one retailer benefits from the action of another without paying for the benefit accrued and

[175] Frank Mathewson & Ralph Winter. (1998) 'The Law and Economics of Resale Price Maintenance'. *Review of Industrial Organization*, **13**:57-84, p.70-74.
[176] Id.p.74.

emerges as follows. Retailer A provides pre-sale service and information (such as how to use the goods, alternative offers, free tests, etc.) to customers and must cover this cost by adding to the price of goods sold. Retailer B doesn't provide pre-sale service and information dissemination about the product rather possesses discount store and offers the product at cheaper price. Consumers after having full-service from service rendering retailer about the available offers, choices, free test and possessing pertinent information about the product they go to nearby retailers who don't provide and buy the product.

This free-riding by both consumer and retailer discourage service providing retailer and consumers who value the service find no provider of service. This demands the intervention of manufacturer to impose MRPM to curb the free-riding problem and protecting exit of retailers who provide service valued by customers. Thus, MRPM prevents free-riding problem observed among retailers.

The free-riding argument is based on the assumption that customers value of pre-sales and pre-purchase information. And this is not a blanket endorsement of free-riding justification for every product. Free-riding justification is convincing for products possessing the attributes of experience and credence. The value of service provision increases in experience goods whereby the consumer can adequately evaluate after they only buy and use and in credence goods where consumers can't evaluate the quality of products even after consuming.[177]

There is a risk of purchasing without being exposed to information about the product. The degree of risk of consumer injury from non-informational promotion increase from search goods to experience goods and from experience goods to credence goods along the scale line.[178] Therefore, for experience and credence goods for which information promotion is valued and necessary and free-riding retailers should be discouraged by MRPM. Consumers wouldn't go away after fully

[177] Warren S. Grimes. (1992) 'Spiff, Polish, and Consumer Demand Quality: Vertical Price Restraints Revisited'. *California Law Review*, **80**(4):815-855, p.825.
[178] Id.p.827.

benefiting from the service and information promotion when the free-riding retailers are discouraged. When the market is competitive imposing MRPM to curb free-riding retailers shouldn't be condemned as long as consumers could switch to substitutes when MRPM imposed.

However, the advent of internet retailing significantly changes how consumers purchase goods.[179] Online retailer provides pre-purchase information to consumers and these consumers go to brick-and-mortar stores for products and reduces need for in-person retailer service.[180] Lao argued that free-riding occurs in opposite direction whereby customers benefit from internet retailer's service and purchase from brick-and-mortar retailer and on top of that internet retailer don't support MRPM, so that, internet retailing weakens free-riding explanation for MRPM.[181]

This Article submits that internet retailing service justification is not persuasive to deny MRPM justification in the Ethiopian context. In internet coverage, Ethiopia, as the following data speak, has a bleak picture. Ethiopia is grouped under "higher barriers across the board" where the country overwhelmed by obstacles to expanding internet adoption; the offline population is illiterate and rural, has very low internet penetration rate, 50% of the offline population is literate and 61% of the population is illiterate.[182]

In addition, Ethiopia ranked 80 out of 81 countries in terms of internet's contribution to development, 92 million out of 94 population non-internet users makes half of total offline population in East Africa; urban internet access in Ethiopia is the lowest among African peers. Ethiopian

[179] Lao (supra note 45) p.475.
[180] Id.p.475-476.
[181] Ibid.
[182] McKinsey & Company (2014) 'Offline and Falling Behind: Barriers to Internet Adoption', *Report*, p.6-42. Available at https://www.google.de/search?biw=1366&bih=628&q=related:www.mckinsey.com/~/media/McKinsey/dotcom/client_service/High%2520Tech/PDFs/Offline_and_falling_behind_Barriers_to_Internet_adoption.ashx+McKinsey+%26+Company+(2014)+%E2%80%98Offline+and+Falling+Behind:+Barriers+to+Internet+Adoption%E2%80%99&tbo=1&sa=X&ved=0ahUKEwjXtLqanvrNAhWfHsAKHe5pClwQHwgmMAE&dpr=1 (Accessed 20 July 2016)

consumers yet to benefit from the internet retailing as online retail penetration is 0.4% and Ethiopia faces daunting challenge in realizing internet penetration.[183]

4.3.4 MRPM as a Tool to Align Incentive Incompatibility

Agency relationship bore externalities which can be tackled by vertical restraints. However, in the absence of free-riding[184] (externalities), vertical restraint is used to align engaged parties' interests.

Retailers are not reaping the benefit from providing service and information promotion; hence, manufacturer devises incentive design to compensate retailers.[185] Retailers for increased service and information promotion of products should be incentivised by having sufficient margin to cover the cost they incurred. Retailers demand minimum expected return from the service they rendered and information promotion about the product and otherwise leads to dropping distribution of products belonging to manufacturer.[186] To ward off distribution drop; to encourage retailers to provide service and promote information about the product and retain their valued service, manufacturer employ MRPM to align incentives.

Recommendation

Competition law is recent phenomenon to Ethiopia. The first proclamation, TPP stated in the preamble its objectives were to regulate anti-competitive practices to maximize economic-efficiency and social-welfare. TPP allows exceptions to anticompetitive practices as long as "the advantages to the nation are greater than the disadvantages". TPCPP, heralded the advent of vertical restraint and explicit recognition of MRPM. Exception is allowed as long as efficiency outweighs detrimental effect.

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[183] Id.p.67-72.

[184] Benjamin Klein. (2009) 'Competitive Resale Price Maintenance in the Absence of Free Riding'. *Antitrust Law Journal*, **76**(2):431-481, p.434.

[185] Id.p.436.

[186] Ibid.

Effect-based approach (rule of reason) has been and is a justification in Ethiopia and TCCP emphasizes efficiency on a number of occasions. TCCP contains vertical-restraint and prohibits MRPM entirely (per se illegal) and no exception is allowed even though efficiency justification exists. Non-price-vertical-restraints are treated more favourably and are generally subject to a rule of reason. Vertical-restraints are substitutes for one another which means prohibition of MRPM induces firms to utilize such as exclusive territories and contractual arrangements. This makes competition authority sole deciding body as to distribution-methods. On top of that naked horizontal agreements are blessed exceptionally as long as efficiency defense exists. A fortiori, MRPM should be assessed under rule of reason.

Dictated by normative analysis of law and economics that takes efficiency as objective normative criterion for evaluating laws; this Article endorses MRPM should be assessed under rule of reason when economic efficiency exists. The Article pleas for repeal of per se MRPM prohibition and making MRPM assessed under rule of reason. It argued for the endorsement of MRPM under rule of reason evaluation in case of experience and credence goods.

This Article finds no convincing economic justifications why TCCP is hostile to MRPM and denies economic efficiency defences in exceptional circumstances. This might be related to neoclassical economy concept that measures consumer surplus in price terms that concerns on distributive justice aspect that shifts wealth in favour of consumers rather than producing total wealth. Total welfare unlike consumer welfare is the sum of consumer surplus and producer surplus and indifferent to distributional justice.