

# Antitrust Law Blog

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## **Agency Relationship Between Pesticide Manufacturers and Distributors Exterminated Allegations of Resale Price Maintenance**

On March 24, 2009, the Fourth Circuit Court of Appeals affirmed summary judgment for defendant pesticide manufacturers, dismissing allegations that the manufacturers conspired with their distributors to set minimum resale prices. The Court affirmed a finding that a genuine agency relationship existed between the manufacturers and their distributors, which precluded the existence of an agreement under the Sherman Act. *Valuepest.com of Charlotte, Inc. v. Bayer Corp.* 2009 WL 756901 (4th Cir. Mar. 24, 2009).

### **Background**

In 1996, defendants Bayer Crop Science LP and Bayer Corp. (“Bayer”) introduced Premise, a “non-repellent” liquid termiticide. Unlike previous liquid termiticides which only repelled termites, Premise was used to create a poisonous barrier around a structure that could be carried by termites and would likely spread to the entire colony. Bayer initially sold Premise products to the distributors of its other pesticide products who would then resell the products to pest control services, including plaintiffs.

Then, in 2000, Aventis CropScience, L.P. introduced Termidor, a new non-repellant termiticide. Aventis initially sold Termidor directly to pest control services, but then started using distributors pursuant to non-exclusive agency agreements. Under the agency agreements, Aventis was the seller of Termidor and retained title to the Termidor until it was sold to pest controllers. The distributor agent facilitated the transactions and received commissions for the sales. Under the agency agreement, Aventis set the price at which Termidor was sold to pest controllers, who had formerly been the distributors' customers.

The Aventis agency arrangements were more profitable to distributors than Bayer’s distribution method. Concerned that distributors would choose to distribute Termidor over Premise, Bayer began selling Premise in 2001 through an agency program similar to that used by Aventis. Bayer would retain title to the Premise and set the retail prices, and the distributors would receive a fixed commission for each sale. In 2003, Aventis divested its assets related to Termidor to BASF Corp, who became the assignee of the agency contracts for Termidor and continued to sell Termidor using agency agreements.

On April 25, 2005, Valuepest.com (joined later by other pest control services) filed a class action lawsuit alleging that Bayer, BASF Corp, and other defendants illegally entered into a vertical conspiracy with their distributors to set minimum resale prices of their respective termiticide products in violation of Section 1 of the Sherman Act, 15 U.S.C. § 1. The common antitrust terminology for these alleged practices is "vertical price fixing" or "resale price maintenance." Plaintiffs did not allege a horizontal conspiracy among the manufacturing defendants.

### **Genuine "Agency Defense" to Minimum Resale Price Maintenance Claim**

The district court granted summary judgment for defendants, finding that the manufacturers appointed their distributors as agents to sell their products and such "genuine agency relationships" precluded the finding of a combination, conspiracy, or agreement between separate entities as required under the Sherman Act. Plaintiffs appealed to the Fourth Circuit, arguing that the "agency defense" under *U.S. v. General Electric Co.*, 272 U.S. 476 (1926) was implicitly overruled by the Supreme Court in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007). In the alternative, plaintiffs argued that the agency relationships between defendants and their distributors were a sham. The Court of Appeals affirmed, holding that the agency agreements defeated plaintiffs' claim that a conspiracy existed in violation of the antitrust laws.

*U.S. v. General Electric Co.*, 272 U.S. 476 (1926) originated the agency defense to liability for resale price maintenance. That case involved an allegation of resale price maintenance by a lamp manufacturer (General Electric) and its network of distributors. The court examined the terms of the contracts between General Electric and its distributors and found that General Electric was selling its lamps directly to consumers via agents, rather than selling them to the distributors and requiring the distributors to resell them at a fixed price. The court reasoned that a manufacturer has the right to sell its products on whatever terms it wants, and it is only when the manufacturer adopts a combination with others, that the Sherman Act is implicated. The court held that a manufacturer may lawfully set minimum prices for its products when there is a genuine principal-agent relationship between the manufacturer and its distributors.

The *Valuepest* court rejected plaintiff's argument that *Leegin* implicitly overruled the agency defense in *General Electric*, finding that *General Electric* and *Leegin* deal with two separate elements under Section 1 of the Sherman Act and their holdings stand independently of each other. The court explained that a violation of Section 1 requires two elements: (1) a contract, combination, or conspiracy; (2) that imposed an unreasonable restraint of trade. *General Electric* concerned what facts constituted the first element of Section 1 in resale price maintenance claims – the existence of a contract, combination, or conspiracy. *Leegin*, by contrast, addressed a question under the second element of Section 1 – whether a resale price maintenance agreement, once established, should be considered *per se* unlawful or analyzed under a rule of reason.

*Leegin* overturned longstanding precedent that had held that a minimum resale price maintenance agreement was a *per se* unlawful restraint of trade, and instead held that such an agreement was subject to a rule of reason analysis, considering factors such as information about the business, the nature of the restraint, and market power. Plaintiffs argued that *Leegin* required an analysis of those factors even where a genuine agency relationship existed.

The court dismissed this argument, finding that Leegin applies only after the existence of an agreement had been proven, and General Electric held that a principal-agent relationship is not an agreement for antitrust purposes. The court explained that Leegin would only be relevant if plaintiffs could prove their alternative argument, that the agency relationships claimed by defendants were a sham.

### **Plaintiffs' Alternative Argument that the Agency Agreements were a Sham**

A genuine agency agreement means there is no combination or conspiracy in violation of the antitrust laws. To determine whether the distribution arrangements used by defendants constituted an agreement under Section 1, the court stated that the most important factor was how the parties allocated the business risks. Both defendants Bayer and BASF retained title of their respective termiticide products while they were in the distributors' possession, and the agreements specified that defendants bore the risk until they were delivered to the pest controllers. Defendants were responsible for economic losses due to non-paying pest controllers. The agreements further specified that the distributors were to store the termiticides separately from their own property and label them as belonging to defendants. The court noted that when losses actually occurred, defendants wrote off the losses.

The court also found it important that the defendants used the agency sales method for legitimate business reasons. When Termidor was first introduced, Aventis implemented the agency method to retain more control over how its new product was presented to pest controllers. Defendant Bayer later switched to an agency method to sell Premise in order to stay competitive because distributors preferred the agency method and the commissions they received. Finally, the court acknowledged that there was no evidence that the agency agreements were the product of any coercion by defendants. The court found that the facts indicated the existence of a genuine agency relationship and affirmed summary judgment for the defendants.

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