

Discounting, Bicycles, and the Supreme Court

Last fall, I went to buy my first true road bike as an adult. I test rode half a dozen bikes and eventually settled on either a LeMond Versailles half-carbon frame or a Giant alloy frame. The problem was that I liked the LeMond better, but the Giant was about \$200 cheaper and more in my price range. So I asked the dealer if I could have the LeMond for the price of the Giant. He told me no because he had a contract with the manufacturer which prohibited him from discounting the bike any further than he already had and that he could lose the line if he went below that price.

Had it been even six months earlier, I could have told him indignantly that such agreements were per se illegal under the federal antitrust laws as a forbidden form of price fixing. But now I couldn't. The Supreme Court in June 2007 overturned 100 years of precedent and held for the first time that such vertical price fixing agreements (also called resale price maintenance) were no longer always illegal, but now would be subject to a case-by-case analysis depending on the market power of the manufacturer and the other facts of the case.

This is bad news for bike shoppers. The basic thrust of the 5-4 Supreme Court decision is that vertical price fixing is a way for manufacturers to reward dealers who have nice clean shops, offer good service and repair, and otherwise have knowledgeable sales staff. That's not a bad thing, but it hurts any consumer who does not take advantage of any of these features or who cares first and foremost about price. Allowing vertical price fixing also prevents so-called "free riding" where customers go to the "good" dealers and pump them for information and literally free rides, and then buy somewhere else. Such minimum resale price agreement will now only be illegal when the manufacturer has such a high market share that consumers have no other options to turn to so that a manufacturer could successfully raise price over the long haul.

Under the new case-by-case approach outlined by the Supreme Court, such contracts will rarely be illegal in the bike industry and manufacturers will be more likely to cut off dealers who don't stick to the pricing requirements. No bicycle manufacturer appears to have that significant a share of the industry. There are numerous other brands that consumers can turn to, but if those firms also implement vertical minimum price policies with their dealers a very anticompetitive outcome is possible.

All is not doom and gloom however. Senator Herb Kohl of Wisconsin has introduced federal legislation that would reverse the Supreme Court case that changed the long standing rules barring this practice. In addition, a majority of the states still bar such vertical price fixing under state law. Finally, the lower courts are just beginning to formulate guidelines for when such agreements will be illegal under the new case-by-case approach under the federal antitrust laws. Manufacturers in most industries are taking a wait and see approach before adding, toughening, or enforcing such agreements with dealers.

In the meantime, here are five tips to cushion the impact of last year's Supreme Court ruling:

- 1) Continue to comparison shop. Not all manufacturers impose such minimum price requirements and not all dealers comply with them. It may be a breach of contract for them to discount below their sales price, but that is their problem, not yours.
- 2) Substitute comparable brands. Manufacturers are still forbidden to agree on price among themselves (as opposed with their dealers). If you can be flexible about the brand and the manufacturer you have a greater opportunity for reduced prices then if you stick with a single brand where the manufacturer can control the retail price.
- 3) Buy from out-of-state or through the internet. Take advantage of dealers located in states where the local law hasn't changed and manufacturers cannot tell independent dealers what prices to charge. What's more, you normally save the sales tax, which is another significant discount depending on where you are located.
- 4) Buy used. Once you buy a bicycle or any other physical object, it's yours and you can resell it for whatever you wish. The new owner is not affected by any contract between the manufacturer and the dealer. Deep discounts will thus be available on used bikes through E-bay, Craig's List, the want ads, or from friends and neighbors. There are obviously many hazards to buying used, but getting stuck with the manufacturer's minimum sales price isn't one of them.
- 5) Buy a bundle. If you must have that brand from that shop and the dealer won't budge on price, see if they won't throw in a little something extra as a substitute for not being able to discount the bike itself. Most bike shops sell apparel, helmets, accessories, parts, energy bars, and have their own service departments. Many of these items will not be subject to minimum resale prices and **if** you were going to buy something else anyway, the dealer may be able to discount those items even if they won't bargain on the bike. Even better, the service department should normally belong to the dealer and not be subject to any pricing limitations on future service and tuneups.

As for me, I offered the guy cash if he knocked \$200 off the price. He took it.

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