

## THE ANTI-COMPETITIVE EFFECTS AND ANTITRUST IMPLICATIONS OF CATEGORY MANAGEMENT AND CATEGORY CAPTAINS OF CONSUMER PRODUCTS

LEO S. CARAMELI, JR.\*

### INTRODUCTION

Throughout the 1990s, the retail sale of consumer product goods in the United States underwent a sea change. Grocers merged with other grocers, leading to increased market concentration.<sup>1</sup> Controlling more shelf space than ever before, these new mega-grocers now possess proportionally greater influence over consumer product manufacturers.<sup>2</sup> Manufacturers have responded with strategies designed to strengthen their relationships<sup>3</sup> with the retailers, offering numerous services along with the products they sell.<sup>4</sup> One frequent response is

\* J.D., Chicago-Kent College of Law, Illinois Institute of Technology, 2004; B.S., Business Economics and Management Information Systems, The Miami University, 1996. I would like to thank my wife Kelley for her patience and support—without her, I never would have completed this Note. I would also like to thank Professor Christopher R. Leslie for his encouragement and suggestions. Finally, thanks to Kelly M. Neff, who provided invaluable feedback.

1. Hayden Stewart & Steve Martinez, *Innovation by Food Companies Key to Growth and Profitability* FOOD REV., May 1, 2002, at 28, 30 (“The nationwide market share of the four largest grocery chains reached 27.4 percent in 2000, compared with 17.0 percent in 1987.”), available at <http://www.ers.usda.gov/publications/FoodReview/May2002/frvol25i1f.pdf>. Other sources place the 2000 market share of the top four supermarkets closer to 42 percent. Federal Trade Commission, *Workshop on Slotting Allowances: Transcript of June 1, 2000 Proceedings* 388 (testimony of Daniel Savrin), available at <http://www.ftc.gov/bc/slotting/slotting61.pdf> (last visited Mar. 22, 2004) [hereinafter *FTC Slotting Day 2*]. One author even argues that the American grocery market is structured in such a way that market concentration should be addressed on a regional basis, yielding a four-firm market concentration increase from 49.3 percent in 1958 to 62.4 percent in 1987, based upon metropolitan areas of more than one million people. William H. Borghesani, Jr. et al., *Food for Thought: The Emergence of Power Buyers and its Challenge to Competition Analysis*, 4 STAN. J. L., BUS. & FIN. 39, 45–46 (1999).

2. In addition to possessing supra-competitive market power, large retailers also control manufacturers’ access to consumers. See Borghesani, Jr. et al., *supra* note 1, at 42–43.

3. An alternative perspective is that manufacturers respond not to strengthen a relationship, but as a response to explicit or implied threats by a retailer to sever or substantially weaken an existing relationship. Certainly large retailers have been known to apply onerous pressure on suppliers. See, e.g., *id.* at 50–51.

4. See Stewart & Martinez, *supra* note 1, at 28.

to provide Category Management services free to certain retailers that purchase the manufacturers' products.<sup>5</sup>

Category Management is a business practice by which a retailer plans its strategy on a product-category level rather than on a brand-by-brand basis.<sup>6</sup> Products are grouped into commonly understood categories such as toothpaste, shampoo, or more broadly, hair care. One main objective of Category Management is to assess consumer demand at the category level and stock store shelves in a way that best reflects that demand.<sup>7</sup> Once the Category Manager determines who shops at the targeted retailer and what products those consumers wish to purchase, they can design the category appropriately.<sup>8</sup>

Countless variables influence consumer purchasing decisions, and Category Management focuses on those that a retailer can most effectively leverage to drive sales. The four main decision points, or components, of Category Management are choosing the most appropriate assortment, placement, pricing,<sup>9</sup> and promotion of products carried at the store level.<sup>10</sup>

5. Al Urbanski, *Can of Corn: With a Steely Focus on Efficiency and Functionality, Del Monte Makes Category Management Seem Simpler Than It Is*, SUPERMARKET BUS., Nov. 1, 2001, at S10 (explaining that at Del Monte, Category Management is defined as “[t]he combining of reasonably substitutable items into a single group that can be merchandised, priced, and promoted to achieve specific financial and other results.”).

6. Brandon Copple, *Shelf-Determination: Under Betsy Holden, Kraft Foods is Winning the War of the Aisles*, FORBES, Apr. 15, 2002, at 130, 140.

7. Thomas K. Arnold, *Wal-Mart's Captain of Home Video: Warner Has Acted as Chain's Chief Adviser on Home Entertainment Since April 2001*, VIDEO STORE, Apr. 14, 2002, at 1, 8.

8. *Id.*

9. The idea of a manufacturer making price recommendations to a retailer may be troublesome to an antitrust academic, but it does not appear that the business world shares the same fears. For instance, a recent article recommended that Category Captains seize greater control over pricing decisions at the retail level. See generally John Phipps, *Pricing For The 21st Century: Winning the Price-Point Battle Profitably*, SUPERMARKET NEWS, Jul. 16, 2001, at 22s (“As category captains, manufacturers have expanded their relationships with retailers by taking on the role of trusted advisers in all these areas. Until now, pricing has been conspicuously absent from that list. . . . As supermarkets learn to use pricing more precisely to manage sales and profits the category captain role will necessarily also incorporate this capability.”). Moreover, in his statement before Congress, Wisconsin Law Professor Peter C. Carstensen indicated that a Category Captain might control all aspects of category decisions for a grocery store chain, including “setting prices.” *Ensuring Competitive and Open Agricultural Markets: Are Meat Packers Abusing Market Power?*, Testimony Before the U.S. Senate Comm. on the Judiciary, 107th Cong. (Aug. 23, 2002) (testimony of Peter C. Carstensen, Professor of Law, Wisconsin Law School), available at [http://judiciary.senate.gov/print\\_testimony.cfm?id=382&wit\\_id=840](http://judiciary.senate.gov/print_testimony.cfm?id=382&wit_id=840); see also Stewart & Martinez, *supra* note 1, at 28 (noting that Category Captains may at times “suggest[] retail prices” to retailers); Copple, *supra* note 6, at 142 (describing Kraft’s admitted practice of instructing retailers “what to charge for each brand.”). Furthermore, according to Robert L. Steiner, the category plans that Category Captains submit can include pricing recommendations. *FTC Slotting Day 2*, *supra* note 1, at 367.

10. Product promotion is simply a form of advertising or marketing.

Through focus on these four components, Category Management has transformed the way grocers sell consumer products. What was once trial and error is now a sophisticated marketing science.<sup>11</sup> Consumer desires, behaviors, values, beliefs, social norms, and preferences are closely studied and analyzed.<sup>12</sup> The findings from these studies are then reflected not only in the features of the products consumers purchase, but in the layout and design of supermarkets as well. The resulting product assortment, price, promotion, and placement have a dramatic effect on consumer decisions at the point of purchase.<sup>13</sup>

Because Category Management strategy and implementation is critical to a retailer's performance, it may be surprising to learn that some retailers rely heavily upon manufacturers to make these decisions for them.<sup>14</sup> Despite recent mergers and growth, most supermarket chains still spend relatively modest amounts on marketing at the store level,<sup>15</sup> and rarely possess the staffing and expertise necessary to make educated Category Management decisions for themselves.<sup>16</sup> While retailers likely understand that perfecting Category Management planning and implementation is critical to the success and profit-maximizing performance of any given supermarket, they often choose to pass the majority of these decisions along to manufacturers from which the retailers purchase.<sup>17</sup>

Large supermarket chains successfully pass Category Management responsibilities along to manufacturers by appointing "Category

11. See Robert L. Steiner, *Category Management—A Pervasive, New Vertical / Horizontal Format*, ANTITRUST, Spring 2001, at 77, 77–78 (2001). For a brief discussion of how category management works, see Ted Gladson, *Crunch Numbers, Move Products*, AFTERMARKET BUS., May 12, 2003, at 9, available at <http://www.aftermarketbusiness.com/aftermarketbusiness/article/articleDetail.jsp?id=55428> (discussing category management in the auto care business).

12. See generally Pollack Associates, *Supermarkets and Their Shoppers* (2002), <http://www.supermarketalert.com/pdf%20docs/2Shoppers.pdf>.

13. See *infra* note 45.

14. See Copple, *supra* note 6, at 140; see also *infra* notes 175–76 and accompanying text.

15. See Copple, *supra* note 6, at 140.

16. See Steiner, *supra* note 11, at 80. Steiner notes that:

[U]nlike sizeable consumer goods manufacturing firms, even the largest retailing firms have never had big staffs with personnel holding advanced degrees in management, marketing, consumer behavior, statistics, and other relevant skills. And yet supermarkets and other mass purveyors of consumer goods can operate in over 200 categories compared to less than 10 in the Category Captain's firm. So a single Category Manager for the retailer is ordinarily responsible for numerous categories. Even Wal-Mart's Category Managers have sometimes been stretched so thin that they cannot exercise adequate supervision.

*Id.*

17. *Id.*

Captains”<sup>18</sup> to manage a portion of the chain’s Category Management efforts. A Category Captain is a single preferred manufacturer that assumes responsibility for the Category Management planning and implementation for one or more product category at a retail chain. As such, the Category Captain, and not the retailer, analyzes store needs and offers Category Management recommendations and services. For each product category (*e.g.*, toothpaste) the retailer relinquishes exclusive control of Category Management related decisions to the manufacturer that offers the best package of services.<sup>19</sup> Typically the services include full-time personnel to produce “plan-o-grams,”<sup>20</sup> recommend prices,<sup>21</sup> manage promotional activities,<sup>22</sup> reset shelves and clean stores,<sup>23</sup> and purchase and analyze costly market data.<sup>24</sup> These are the primary tasks that go into making and executing informed Category Management decisions.

This arrangement often results in business relationships conducive to opportunistic behavior by the Category Captain. For instance, in almost every potential Category Captain arrangement the chosen manufacturer performs Category Management tasks not only for its own brands, but for those of competing manufacturers as well. Furthermore, the same manufacturer may also serve as Category Captain for multiple retailers competing in the same market.<sup>25</sup> Even more surprising, despite the significant effort and expense that a manufacturer must expend to serve as Category Captain and the undeniable value conferred to the retailer, sometimes retailers demand a cash payment in exchange for the privilege of serving.<sup>26</sup> As will be

18. *Id.* at 77.

19. Some retail chains reserve the final say in what changes are implemented while others do not; there is a broad spectrum of practices across the industry. See Federal Trade Commission, *Report on the Federal Trade Commission Workshop on Slotting Allowances and Other Marketing Practices in the Grocery Industry* 48 (Feb. 2001), available at <http://www.ftc.gov/os/2001/02/slottingallowancesreportfinal.pdf> [hereinafter *FTC Slotting Final*].

20. See Steiner, *supra* note 11, at 77 (explaining that a “plan-o-gram” is a visual depiction of where each product in a given category should be shelved).

21. See *supra* note 9.

22. Steiner, *supra* note 11, at 77.

23. See Mark Tosh, *Third Party Merchandisers: Who’s Minding the Store?*, *PROGRESSIVE GROCER*, Aug. 1998, at 89, 89–90 (discussing the emerging debate over which party will fund store shelf resetting activities).

24. See Copple, *supra* note 6, at 142.

25. See Urbanski, *supra* note 5. Del Monte claims to serve as Category Captain at almost all of the top twenty-five wholesalers and retailers nationwide. *Id.*

26. David Merrefield, *Your Payment, My Captain?*, *SUPERMARKET NEWS*, June 10, 1996, at 2 (describing “captaincy fees for Category Management partnerships between supermarkets and food manufacturers”). In fact, in 1996 a national drug chain was charging \$100,000 to serve as captain. Richard Turcsik, *Go Beyond ECR, Consultant Urges*, *SUPERMARKET NEWS*, Dec.

discussed, *infra* Part II, these payments may by themselves signal anti-trust concerns.

Intuitively the Category Captain relationship is like the “fox guarding [the] henhouse.”<sup>27</sup> Choosing which products to sell and how to price, shelve, and promote them is a job that most logically and traditionally belongs to the retailer itself, and not a manufacturer. After all, the manufacturer is concerned primarily with its own brands and has a vested interest in seeing competing products fail.<sup>28</sup> The retailer, on the other hand, has a vested interest in maximizing overall profit in its stores, regardless of brand.<sup>29</sup> It seems, then, that there is a fundamental difference between a Category Captain’s business goals

30, 1996, at 23. When one begins to consider that not only are manufacturers spending a good deal of resources to manage a category for a retailer, but are paying for the “privilege” of doing so, it begins to appear as though retailers may be exerting monopsony-like influence even over large manufacturers.

27. Copple, *supra* note 6, at 132. Furthermore, at least one retailer has opined that “[s]ome manufacturers and brokers don’t really understand category management, some don’t look at categories without bias and some are not aligning their category strategies to the retailer.” Les Hill, *Challenging an Assumption*, PROGRESSIVE GROCER, Jan. 1, 1997, at 17.

28. According to Don Sussman of Ahold’s Stop & Shop grocery chain, if a manufacturer can displace a competitor’s better selling product, then that manufacturer benefits even if the store does not. Federal Trade Commission, *Workshop on Slotting Allowances: Transcript of May 31, 2000 Proceedings* 90, available at <http://www.ftc.gov/bc/slotting/slotting531.pdf> [hereinafter *FTC Slotting Day 1*]. The manufacturer likely also has an interest in the overall profitability and financial health of its retailers, but all else being equal, the manufacturer would want to see as much of that retailer’s profits come from the manufacturer’s own products.

29. Al Urbanski, *Captains Courageous*, SUPERMARKET BUS., Nov. 1, 2001, at S3 (observing that “Retailers care not whether a category captain grows its own share; retailers care whether category captains grow their entire categories.”). Certainly the retailer does have a vested interest in selling more of the most profitable brands it carries. Nevertheless, there are valid business reasons that may motivate a retailer to stock less profitable brands. For instance, Ukrop’s Kevin Hade indicates that his grocery stores will carry an item that does not appear good on paper, but which his highest volume shoppers tend to purchase. *FTC Slotting Day 2*, *supra* note 1, at 339. In addition, retailers frequently offer certain items at unusually low prices simply to draw consumers into the store, hoping they will purchase other items as well. See Alexander Coolidge, *Supermarkets Drive Traffic with Lower Gas Prices*, CINCINNATI POST, Sep. 5, 2003, at C7, available at <http://www.cincypost.com/2003/09/05/krogergas090503.html> (noting that “gasoline is a way to drive customers into [] stores to buy other things”). Still, it seems evident that the underlying motivation for stocking these less profitable brands is to maximize total profit in the category or retail store as a whole. The manufacturer, however, would not necessarily share the same perspective and goal. The manufacturer, it seems, would be interested in these ancillary products only to the extent that their absence would prevent a consumer from purchasing the manufacturer’s own product at that or any other retailer in the relevant market. While it may seem difficult to reconcile the inherent conflict in a Category Captain that desires only to maximize its own brand sales, with a retailer that seeks to maximize category profits regardless of brand, a recent study supports the conclusion that manufacturers may be providing Category Captain services only due to pressure from retailers. The study notes that while Category Management has proven profitable to retailers, “both consumers and brand owners lose out. . . . Consumers pay higher prices while suppliers get lower prices.” Tim Ambler, *Category Management is Best Deployed for Brand Positioning*, MARKETING, Nov. 29, 2001, at 18.

and those of the retailer it serves. One logical conclusion, therefore, is that the retailer is the more appropriate party to perform category management tasks.<sup>30</sup>

Moreover, the Category Captain practice becomes even more suspicious when one considers that a single manufacturer may be making all of a retailer's decisions regarding competing manufacturers' products.<sup>31</sup> In the words of Commissioner Thomas Leary of the Federal Trade Commission, "[a]s an antitrust matter, it seems rather strange that you'd have one company advising a store on how to handle the product of its competitors."<sup>32</sup> Indeed, this practice appears even stranger when one considers that companies are recommending retail prices.

Certainly it is possible that a Category Captain will perform its duty with no other goal than to do what is best for the supermarket and the consumer, attempting only to reap the benefits of a fine-tuned supermarket by maximizing the efficiency of the product category as a whole.<sup>33</sup> But there are complications to this paradigm that merit serious consideration from academia and the court system: the anticompetitive potential and reality, and antitrust implications of Category Management and Captain practices.

This Note focuses on Category Captains and Category Management as they apply to the consumer product industry, primarily within the grocery store segment.<sup>34</sup> In their most innocuous implementations,

30. Even if a manufacturer possesses specialized knowledge of a given category, the final decision still logically falls on the retailer.

31. Steiner, *supra* note 11, at 77.

32. Cople, *supra* note 6, at 136.

33. There are certainly hypothetical examples of stores in which revamping poorly designed categories may yield an overall increase in sales for the entire category. Naturally, the manufacturer with the dominant product in a category will see a benefit from doing category management work, despite also providing a benefit to its competitors. For instance, Kraft Foods has demonstrated that by properly shelving pourable and spoonable salad dressings, stores can realize a sales volume increase in both. See John Karolefski, *The New Category Captain*, SUPERMARKET NEWS, June 30, 2003, at 53, 56. Still, it is simply not rational for one manufacturer to spend its money to provide these services only to benefit its competitors in an equal amount. At minimum, the manufacturer must recoup its investment plus any amount of revenue that it may lose to its competitors in the process in order to justify the effort. If this does not occur, the behavior is not likely rational. In such instances, it would be wise to ask whether the manufacturer is recouping its investment in some other way, or whether the manufacturer has been unduly coerced into providing services to the retailer.

34. This Note focuses on the grocery segment of consumer products retailing because of the recent wave of mergers and the corresponding increase in market concentration within the segment. To the extent possible the author has limited discussion to grocery stores. Nevertheless, commentary regarding Category Captain practices in other market segments, e.g., mass retailers such as Wal-Mart or video stores, have been included to help complete gaps in research. Antitrust concerns are likely equally as valid in these other market segments.

Category Captaincies probably do not violate antitrust laws. Category Management as retailers and manufacturers sometimes practice it, however, can help facilitate anticompetitive conduct by one manufacturer intended to exclude other manufacturers' products from the marketplace.<sup>35</sup> It may also lead to collusion amongst grocers that act to restrain competition. Finally, Category Captaincies as they are often implemented present significant opportunity for larger retailers to coerce Category Management services from manufacturers that a manufacturer does not, or cannot, offer smaller stores on proportionally equal terms, thus presenting Robinson-Patman Act concerns.<sup>36</sup>

Part I of this Note provides a brief discussion of the goals and purpose of antitrust law. Those familiar with antitrust law may wish to proceed to Part II.<sup>37</sup> Part II of this Note presents an overview of Category Management, Category Captains, and corresponding practices. Part III focuses on potential violations of Sections 1 and 2 of the Sherman Act stemming from certain implementations of Category Management and Category Captain practices. This part details the potential for collusive resale price maintenance agreements, and for misrepresentation and tampering by a malicious Category Captain. Part IV of this Note analyzes potential violations of Section 2 of the Robinson-Patman Act that may result from common implementations of these practices. Most importantly, this section addresses the need for manufacturers to offer all services to competing retailers on proportionally equal terms. Part V of this Note presents recommendations for altering category management implementations in a way that retains legitimate benefits to manufacturers and retailers, but which may reduce the risk of violating antitrust laws.

35. See, e.g., *Conwood Co., L.P. v. United States Tobacco Co.*, 290 F.3d 768 (6th Cir. 2002). In *Conwood*, one Category Captain destroyed shelf displays and hid product of a competitor. *Id.* at 778. It also misled retailers as to the product assortment and shelf placement best for the retailer. *Id.* at 776.

36. Although the Robinson-Patman Act receives much criticism and is not heavily litigated, the FTC has expressed a willingness to enforce the act if a proper challenge is filed. See *FTC Slotting Day 2*, *supra* note 1, at 460 (comments of David Balto, then Assistant Director for Policy and Evaluation in the FTC's Bureau of Competition).

37. Part I makes no attempt to debate the various schools of antitrust, nor the relative strengths of Cournot, Stigler, Bain, or even Posner. The analysis presented in this Note is intended to provide an overview of an emerging antitrust concern and assumes only that antitrust law is necessary on at least some level to maintain an economic structure conducive to competitive behavior. No attempt is made to choose a specific model of oligopolistic competition. To the extent that any viewpoint is implied, such an implication was unintentional.

## I. THE GOALS AND PURPOSE OF ANTITRUST LAW

Antitrust, as with many or most other bodies of law, emerged as a way to help achieve an overriding goal considered by society as beneficial. With criminal law, society has rules to deter and punish criminals, hoping to make our lives a bit safer. For business it has accounting laws, hoping to provide investors the opportunity to make educated investment decisions. At the intersection of business and criminal laws, society also has antitrust. Antitrust laws were instituted to ensure that the American marketplace remained a competitive one.<sup>38</sup>

Nevertheless, it is certainly true that competition is not the only way to allocate societal resources. Societies across the globe survive and sometimes even prosper with varying degrees of non-competitive, more centrally controlled market structures. But America has consistently espoused the largess of capitalism, a necessary part of which is an economy where competition exists to govern behavior.<sup>39</sup>

Just as a safe world requires criminal laws and enforcement, a competitive economy requires laws to encourage those with a proclivity to misbehave to act competitively. This is where antitrust laws come in. Without these laws, society would have fewer means by which to regulate the behavior of those whose views do not agree with the broader societal vision—with those who decide it is in their own best interest to eliminate their competition not by building a better or cheaper mousetrap, but instead through incorrigible and nefarious acts. The basic tenet of antitrust law's goals, therefore, is to create a system whereby economic power in any given industry is spread out among numerous competitors.<sup>40</sup> This, in turn, ensures that

38. See Harry S. Gerla, *Restoring Rivalry as a Central Concept in Antitrust Law*, 75 NEB. L. REV. 209 (1996) (explaining that antitrust exists to maintain an environment in which rivalry between firms can flourish).

39. A competitive marketplace is not to be confused with free and unrestrained "competition." A competitive marketplace assumes that every participant has the opportunity to compete based upon the virtue of its product or service, unimpeded by constraints such as price fixing or market collusion. Furthermore, it should be noted that while competition can exist in non-capitalist economies, competition is typically viewed as a necessary condition for market capitalism. See, e.g., Spencer Weber Waller, *Neo-Realism and the International Harmonization of Law: Lessons from Antitrust*, 42 U. KAN. L. REV. 557, 604 (1994) ("Competition policy . . . is the jurisprudence of capitalism, and it speaks to a society's view of the role and the relationship of the individual, the enterprise and the government in a pluralistic society and economy.").

40. See *United States v. Columbia Steel Co.*, 334 U.S. 495, 536 (1948) (Douglas, J., dissenting). Justice Douglas notes that:

The philosophy of the Sherman Act is that [firms with significant market power] should not exist. For all power tends to develop into a government in itself. Power that controls the economy should be in the hands of elected representatives of the people,

no single player leverages its size to the detriment of other, less-powerful firms.

For example, consider a hypothetical widget industry.<sup>41</sup> If widgets are a good that consumers want, or even need, and are willing and able to pay a price that is greater than or equal to the marginal cost of production,<sup>42</sup> then firms will emerge as producers of widgets to meet consumer demand.<sup>43</sup> Assume that some consumers are willing and able to pay between \$1.00 and \$1.10 per widget. Assume also that producers can produce widgets at a marginal cost of \$1.00<sup>44</sup> and that all widgets are of roughly equal quality. In a perfectly competitive economy each producer is a price-taker, meaning it has no ability to influence market price. Therefore, with 1000 manufacturers composing roughly equal shares of the market, it would be quite difficult for one producer to raise its price to \$1.10, even though it is well aware certain consumers value the widget that highly. If that producer did, those consumers would merely purchase a different brand of widgets still selling at \$1.00.

Given the abundance of producers, none if acting alone has the ability to raise its price even as high as \$1.01. To do so, that producer would need some insurance that other producers would also raise prices. Antitrust law exists in part to help make certain that firms do not devise ways to create this insurance by forming cartels, entering collusive pricing arrangements, or devising other disreputable practices.

This is the competitive model in its simplest rendition—every firm fighting for itself, attempting to earn a profit by producing the

not in the hands of an industrial oligarchy. Industrial power should be decentralized. It should be scattered into many hands so that the fortunes of the people will not be dependent on the whim or caprice, the political prejudices, the emotional stability of a few self-appointed men. The fact that they are not vicious men but respectable and social minded is irrelevant. That is the philosophy and the command of the Sherman Act. It is founded on a theory of hostility to the concentration in private hands of power so great that only a government of the people should have it.

*Id.*

41. This is admittedly oversimplified, but is used here as an illustration.

42. Marginal cost is the cost to the manufacturer of producing one additional unit. HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE §1.1b (2d. ed. 1999). Maureen O'Rourke, *Shaping Competition on the Internet: Who Owns Product and Pricing Information?*, 53 VAND. L. REV. 1965, 1968 n.4 (2000). While not truly measurable in a real world sense, marginal cost is useful for theoretical analysis.

43. The consumer's demand curve in a simplified perfectly competitive economy will be horizontal, meaning that price is the same at any level of output. HOVENKAMP, *supra* note 42, at 8.

44. This cost includes, of course, salaries and other production costs.

best product at the lowest possible price. Still, at times firms may prefer to sell at higher margins by either offering a lesser quality product at the same price or the same quality product at a higher price.<sup>45</sup> To achieve this, the firm must find a way to prevent other firms from meeting consumer demand for the higher quality product at the lower price. Short of the previously mentioned collusive agreements, one of the most effective ways to achieve this is by gaining a larger market share and devising ways to make it too costly for others to enter the market. In this scenario, a firm can, indeed, raise its prices because there will not be enough competing firms to produce and sell the less expensive widget, nor will others be able to enter the widget market easily. A firm that achieves both market power and entry barriers can therefore sell its widgets for between \$1.01 and \$1.10. Certainly, this will price some consumers out of the widget market and charge others a greater percentage of their reservation price,<sup>46</sup> but this is not the firm's concern. It is, however, of concern to society.

Antitrust laws seek minimize market power by enforcing a market structure whereby firms must by law compete on the merits of their products or services. When a firm expends its resources for the sole purpose of excluding its competitors to gain market share rather than producing the best product or service at an attractive price, society does not benefit as much as it otherwise would. Certainly, the firm gains, but the industry as a whole is hurt. Society and consumers are as well.

Competition, on the other hand, benefits consumers in several ways. First, price discipline<sup>47</sup> ensures that manufacturers sell goods at the marginal cost of production. This is the lowest price at which a manufacturer can sell and remain profitable. As such, competition ensures that all consumers that value a good at or above this price can purchase the good, thus maximizing societal benefit.<sup>48</sup> Furthermore, competition provides the ancillary benefit of freeing resources of

45. Selling a lesser quality product at a lower price or a higher quality product at a higher price is, of course, legitimate.

46. A person's reservation price is the maximum they are willing to pay. In the current example, some consumers have a reservation price of \$1.00, meaning that they will not purchase a widget at \$1.01. Still, some have a reservation price of \$1.05. When widgets are selling at the competitive price of \$1.00, this consumer is said to have a "consumer surplus" of \$0.05. Nevertheless, this consumer would still buy the widget at a higher price, up to \$1.05.

47. Price discipline means that there are enough rivals competing for a consumer's dollar that each is compelled to keep prices as low as possible.

48. Consumer surplus is essentially the difference between what a consumer pays for a product and the maximum amount they would have been willing to pay.

those who value the good at a price greater than marginal cost to purchase other goods or services. This, of course, benefits society even further. It is for these reasons that antitrust laws seek to maintain a competitive marketplace.

Therefore, seeking to protect consumers from potentially abusive producers, Congress passed the Sherman Act and later the Robinson-Patman Act. In doing so, Congress sought to limit market power and related concerns. Accordingly, antitrust exists to maintain an economy in which firms find it in their best interest to behave competitively. Part II of this Note provides an overview of Category Management and Category Captain practices. Parts III and IV will explain how current antitrust doctrine should be applied to potential anticompetitive behavior that results from these practices. Finally, Part V will present recommendations for implementing the Category Captain relationship in a way that minimizes antitrust concerns.

## II. CATEGORY MANAGEMENT AND CATEGORY CAPTAIN OVERVIEW

### A. *What is Category Management?*

Category Management is a practice by which a retailer decides what products to sell and how to sell them. Faced with limited shelf space, a retailer must choose carefully which products it wishes to offer local consumers. Moreover, retailers must select from a myriad of ways to shelve and price those products. Category Management provides a methodology by which retailers make these decisions, dividing products into easily managed groups known as categories. A category can be as simple as “toothpaste” or as broad as “oral care.”

The most prominent factors that a retailer can leverage to improve category performance are: (1) the assortment of products the store carries; (2) the placement of those individual products on the shelf relative to other products in the category, the placement of entire categories within the store relative to other categories, and how much total shelf space to allot a category and each individual product therein; (3) the price of the product relative to both its reasonable substitutes in the same store and comparable products at other retailers in the same geographic market; and (4) the promotion of the

product.<sup>49</sup> Each of these factors has profound impact on individual consumers' purchasing decisions.<sup>50</sup> For instance, it is well established that moving a product to eye-level has a dramatic effect on how well a product sells.<sup>51</sup>

*B. Category Management and Category Captains—Retailer and Manufacturer Collaboration*

Category Management emerged in the 1990s as an outgrowth of Wal-Mart's<sup>52</sup> efforts to improve the way it partnered with its suppliers.<sup>53</sup> Category Management's predecessor was a form of vertical partnership in which Wal-Mart partnered with individual manufacturers to increase efficiency in its supply chain relationships.<sup>54</sup> Under the previous paradigm, no manufacturer had any influence over any other manufacturer's products.<sup>55</sup> Category Management as implemented by means of a Category Captain, on the other hand, takes these partnerships to the next level by allowing a single manufacturer to control decisions of an entire product category within a given retail chain.<sup>56</sup> In doing so, implementers of Category Management seek to gain efficiencies and influence consumer purchasing behavior at the retail store.<sup>57</sup>

Given the close collaborative relationship that results when a retail chain appoints a Category Captain to manage its stores by product category instead of by individual product or brand, the retailer has

49. See Steiner, *supra* note 11, at 77.

50. See generally Barbara Murray, *Easy Pickings: Independent Stays Ahead in St. Louis by Making Sure Customers Find it Easy to Shop at Schnucks*, SUPERMARKET NEWS, Dec. 17, 2001, at 35. Furthermore, Category Management can result in significant savings for a retailer. For instance, the H.E. Butt Grocery Company claims that Category Management enabled it to save \$12 million annually. See Steiner, *supra* note 11, at 78.

51. See, e.g., Robert L. Steiner, *The Nature and Benefits of National Brand/Private Label Competition* at 12 (working paper presented at Annual Meeting of the American Economic Association, Jan. 5, 2002), available at <http://www.antitrustinstitute.org/recent2/174.pdf>. Steiner points out that "a couple of facings at eye level [will do] more for [a] product than five facings on the bottom shelf" *Id.* (citation omitted) (emphasis removed). The logical conclusion is, therefore, that manufacturers have a vested interest in fighting vigorously to win beneficial placement for their products.

52. See Amanda Berragan, *Category Management Insight: The Love/Hate Relationship*, RETAIL WORLD, Jul. 8, 2002, at 40 (attributing the emergence of Category Management to Wal-Mart's retail efforts).

53. See Steiner, *supra* note 11, at 77.

54. *Id.*

55. *Id.*

56. *Id.*

57. *Id.* at 77-78.

less need to maintain close relationships with multiple manufacturers within a given category.<sup>58</sup> In fact, doing so could lead to confusion or redundancies. The reason for this is that a hypothetical retailer has only one business strategy. To achieve the business objectives of that strategy, there is likely some optimal mix of products the retailer should carry. Each product category also has optimal product placement, promotion, and pricing schemes. Assuming that the advocates of Category Captain relationships are correct in asserting that manufacturers provide only honest and accurate suggestions that will best meet the retailer's business objectives, there is little need for recommendations, data, or input from a second manufacturer. In fact, a retailer does not likely have the staff or the time to meet with each manufacturer within a given category to hear detailed input that is substantially the same. Making time to listen to feedback from multiple manufacturers in a category would, then, be redundant. To prevent this redundancy, some retailers instead choose a single manufacturer to be the "Category Captain," conferring the responsibility to make the retailer's Category Management decisions for an entire category of products.<sup>59</sup>

C. *Only the Big Survive: Which Manufacturers Serve as Category Captains?*

Analyzing consumer behavior and implementing Category Management plans is a costly venture. Nevertheless, retailers sometimes charge a fee for the privilege.<sup>60</sup> Therefore, it is often only the leading manufacturers that can afford to compete for the captaincy.<sup>61</sup> In light of this, the fact that some manufacturers pay for the opportunity to spend their money to perform research and planning for their retailer

58. Category managers at certain chains may look to confirm that all manufacturers agree on the decisions. For some categories at certain retailers, however, the entire category is turned over to the Category Captain. *FTC Slotting Day 2*, *supra* note 1, at 343–44. Furthermore, it has been asserted that even Wal-Mart, with its mammoth size and resources, does not always have sufficient personnel to oversee all of a Category Captain's decisions. *See Steiner*, *supra* note 11, at 80.

59. *See Steiner*, *supra* note 11, at 77. Theoretically, a manufacturer just submits a plan for approval and it is up to the retailer to determine where to go from there. In practice, retailers follow divergent practices. *See generally supra* note 5. Some use a Category Captain and a second manufacturer to check or "validat[e]" the Captain's recommendations. *See Ted Gladson, Merchandising: The Category Captain Steers the Ships*, *AFTERMARKET BUS.*, April 1, 2003, at 8, available at <http://www.aftermarketbusiness.com/aftermarketbusiness/article/articleDetail.jsp?id=51515>.

60. *See Merrefield*, *supra* note 26, at 2.

61. *See infra* note 64.

customer should by itself raise suspicion. In the words of C. Manly Molpus, president and chief executive officer of the Grocery Manufacturers of America,<sup>62</sup>

[t]he fundamental reason to [perform certain Category Management work] . . . is [to facilitate] both partners' understanding of the value of working together to reduce costs so they both become more efficient and more profitable and serve the consumer better. That should drive partnerships, rather than [a requirement to] buy your way into a partnership.<sup>63</sup>

Moreover, even absent an entrance fee, smaller manufacturers may not have the opportunity to serve as Category Captains.<sup>64</sup> This places them in a position less favorable to building and maintaining key relationships with retailers. Likewise, smaller retailers often do not have the clout to demand Category Captain services from a manufacturer,<sup>65</sup> and therefore may be similarly disadvantaged vis-à-vis larger retailers by having to perform Category Management work on their own.

Furthermore, it is safe to assume that, all else being equal, a manufacturer would prefer that a retailer itself perform all necessary Category Management tasks and absorb the corresponding costs. Even in an environment where that is not feasible, however, it is likely that a manufacturer in a competitive marketplace would not see

62. The Grocery Manufacturers of America is a trade group representing grocery manufacturers. See generally About GMA, <http://www.gmabrands.com/about/index.cfm> (last visited March 15, 2004).

63. See Merrefield, *supra* note 26, at 2.

64. The opportunity to serve as Category Captain "goes by default to the dominant manufacturers" in a given category. JUDITH CORSTJENS & MARCEL CORSTJENS, STORE WARS: THE BATTLE FOR MINDSPACE AND SHELFSPACE 291 (1999). In fact, smaller manufacturers often have difficulty getting their products on the store shelf in the first place. See Alby Gallun, *Small Fry Take On Big Brands: Shelf Squeeze; Local Food Makers Facing a Tougher Fight To Win Space in Supermarkets*, CRAIN'S CHI. BUS., Sep. 17, 2001, at 17; see also *FTC Slotting Day 1*, *supra* note 1, at 76-78. (comments of Scott Hannah of Pacific Valley Foods, a small manufacturer. Hannah discusses slotting fees from \$100 to \$300 per store, and aggregate values as high as \$100,000. He notes that, "If you're not going to pay . . . don't bother coming in. It's that pointed."); Steiner, *supra* note 11, at 79. Furthermore, manufacturers with market power may even be able to resist paying a Captainty fee, where smaller manufacturers cannot. See Merrefield, *supra* note 26, at 2. Certainly the manufacturer will still absorb the high cost of providing Category Management services, but reduction or elimination of a Captainty fee can provide still another benefit to a large manufacturer over its smaller competitor.

65. See Robert J. Aalberts & L. Lynn Judd, *Slotting in the Retail Grocery Business: Does it Violate the Public Policy Goal of Protecting Businesses Against Price Discrimination?*, 40 DEPAUL L. REV. 397, 401 (1991) (noting that small, independent grocers have a difficult time competing with large chains).

fit to pay for the right to serve as Category Captain, only to then benefit its competitors as much as it does itself.<sup>66</sup>

One possible motivation for a manufacturer to pay is that it is really purchasing a chance at obtaining monopoly or oligopoly power at the retail level. While it is not likely that a retailer would permit a manufacturer to eliminate heavily demanded products, certainly the Category Captain's products have a better chance of prevailing at the retailer than those of competing manufacturers.<sup>67</sup> A second, likely related, possibility is that in charging a Captaincy fee the retailer is actually seeking to recover a portion of the manufacturer's share of consumer surplus.<sup>68</sup> Under this theory, a retailer is well aware that manufacturers need its commodity, limited shelf space. As such, in exchange for a cash payment, the retailer relinquishes control of the shelf decision-making to a Category Captain. Under this scenario, the Captain pays because it knows that if it does not, its competitor will.

Category Management emerged as a way for producers and retailers to join together to improve retailing strategy. For many logical product groupings, the retailer appoints, sometimes at a fee, a preferred retailer to serve as Category Captain. The Captain then analyzes the product category and makes recommendations on what products the retailer should carry in its stores, and how the retailers should shelve, price, and promote those products. In a textbook implementation, this practice may not present an antitrust problem. Nevertheless, the collaborative and trusting nature of the relationship presents numerous opportunities for antitrust violations.

66. As discussed, *supra note* 33, there are situations where the mere implementation of Category Management will boost performance of an entire category. It is likely safe to assume that the Category Captain's product(s) composes a greater percentage of the category than its competitors and that it will, therefore, experience more net growth. Still, it is difficult to conceive of a scenario in which paying a captaincy fee would not significantly ameliorate that incentive. As such, the manufacturer rationally must derive some benefit worth paying for. Assuming that Category Captains do not seek to give their brands treatment preferential to competitors' brands, then the only remaining benefit worth paying for is a solid relationship with the retailer. Such a relationship, however, likely provides maximum benefits only when the manufacturer can leverage it to the detriment of competitors.

67. See, e.g., William Smyth, *Wild Oats Implements Category Management Program*, SUPERMARKET NEWS, June 28, 1999, at 31. Jim Lee, president of Wild Oats Markets asserts that a "category captain will . . . have the edge in a tie." *Id.* It is not difficult to imagine that in situations that are close (but not a tie), the Captain will still have the edge.

68. Consumer surplus is essentially the difference between what a consumer pays for a product and the maximum amount they would have been willing to pay. The retailer could also achieve this by raising retail prices. In that scenario, however, other retailers could undercut its price and the retailer would lose sales. By charging a Category Captaincy fee, the retailer can maintain the same retail price and keep more of the profits to itself.

The remainder of this Note will explore the potential antitrust complications that may arise from a Category Captain relationship. Part III will explore how potential collusion or other anticompetitive activities facilitated by such arrangements may implicate Sections 1 and 2 of the Sherman Act. Part IV will then consider the Robinson-Patman Act's requirement that Category Captains make services available to all customers on a proportionally equal basis. Finally, Part V will provide recommendations for implementing the Category Captain relationship in a way that minimizes antitrust concerns.

### III. THE IMPLICATIONS OF SECTIONS 1 AND 2 OF THE SHERMAN ACT ON CATEGORY MANAGEMENT AND CATEGORY CAPTAINS

Holding the position of most-favored manufacturer and serving as Category Captain for even one product category within a given supermarket chain affords the chosen manufacturer a significant voice in that retailer's shelf-level decisions.<sup>69</sup> When viewed in light of the sheer size of today's retail chains,<sup>70</sup> the incentive for a manufacturer to contribute resources for a requesting retailer is compelling.<sup>71</sup> Manufacturers by their very nature also have an incentive to maximize sales and market share of their own products to the detriment of their competitors.<sup>72</sup> This incentive, combined with the increased influence resulting from the manufacturer's newfound partnership with the retailer, may entice certain manufacturers to behave in ways that violate the Sherman Act.

69. Some retailers take suggestions from the Category Captain and make their own decisions, while others allow the Category Captain to be the final decision-maker. *See supra* note 19.

70. Leading grocery chain SUPERVALU controls 1,358 retail grocery locations. NCR, *SUPERVALU Selects NCR Self-Checkout; Leading Grocery Chain Installing NCR FastLane*, [http://www.ncr.com/media\\_information/2002/oct/pr102902.htm](http://www.ncr.com/media_information/2002/oct/pr102902.htm) (Oct. 29, 2002). Furthermore, in 2002 chain supermarkets accounted for 65.4 percent of all supermarkets nationwide while independents make up 34.6 percent. Food Marketing Institute, *Facts & Figures: Key Facts: Number of Stores*, [http://www.fmi.org/facts\\_figs/keyfacts/stores.htm](http://www.fmi.org/facts_figs/keyfacts/stores.htm) (May 2003). Nevertheless, chain supermarkets accounted for 82.7 percent of all sales while independents accounted for only 17.3 percent. Food Marketing Institute, *Facts & Figures: Key Facts: Grocery Store Sales*, [http://www.fmi.org/facts\\_figs/keyfacts/grocery.htm](http://www.fmi.org/facts_figs/keyfacts/grocery.htm) (2003); *see also supra* note 1.

71. One would expect there to also be a strong incentive for a manufacturer to decline the opportunity. Theoretically, assuming Category Captains do nothing more than provide category suggestions that are truly in the best interest of the retailer, then there would be a strong disincentive to reject the Category Captain position (or even pay for it) and merely free ride. Only in the unique situation where overall category sales could be legitimately increased in a way that covers the manufacturer-captain's costs and does not lend more to competitors' bottom lines than the captain's would saying yes be rational.

72. *See, e.g., supra* note 28.

Section 1 of the Sherman Act condemns every contract, combination, or conspiracy that unreasonably restrains trade or commerce.<sup>73</sup> Section 2 of the Sherman Act makes it an offense for a company to monopolize, or attempt to monopolize, trade or commerce.<sup>74</sup> This Part will discuss Section 1 violations resulting from resale price maintenance agreements. Furthermore, this Part will also address potential Section 2 violations whereby a Category Captain achieves monopoly power by affirmatively misleading a retailer through inaccurate Category Management advice, or by sabotaging its competitors' in-store Category Management work.

### A. *Sherman Act Section 1*

Consumer goods operate within a combination of two or more markets. The manufacturer first sells the product to a retailer or wholesaler. Thereafter, a retailer eventually sells the product directly to a consumer. Each of these transactions represents a market that ideally behaves competitively to bring consumers goods they desire at the lowest possible price.<sup>75</sup> Category Captaincies can result in an exclusive vertical relationship between a retail chain and a single manufacturer within the subject category.<sup>76</sup> By its very nature, this exclusive arrangement reduces or eliminates competition.<sup>77</sup> Still, the relation-

73. 15 U.S.C. § 1 (2000). Section 1 of the Sherman Act provides that:

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 shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding \$10,000,000 if a corporation, or, if any other person, \$350,000, or by imprisonment not exceeding three years, or by both said punishments, in the discretion of the court.

*Id.*

74. 15 U.S.C. § 2 (2000). Section 2 of the Sherman Act provides that:

Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding \$10,000,000 if a corporation, or, if any other person, \$350,000, or by imprisonment not exceeding three years, or by both said punishments, in the discretion of the court.

*Id.*

75. It is true that to some degree consumer brand loyalty negates some competition at the manufacturer level by rendering a relatively inelastic demand curve. Warren S. Grimes, *Brand Marketing, Intra-brand Competition, and the Multibrand Retailer: The Antitrust Law of Vertical Restraints*, 64 ANTITRUST L.J. 83, 95 (1995). Still, ideally the market remains free for competitors to develop brand loyalty for their own brands.

76. See Steiner, *supra* note 11, at 77-78; see also *supra* note 19.

77. When a given supermarket chain deals with a single Category Captain, competition is reduced or eliminated between manufacturers competing for influence over in-store decision-making.

ship may not necessarily negatively affect the competitive market to the extent necessary to give rise to antitrust concerns. For instance, cooperation between a manufacturer and a retailer can have pro-competitive effects by helping to ensure that the retailer carries a distribution of products most appropriate for local consumers, and that the products are shelved, priced, and promoted in an optimal manner.

There are numerous decisions, however, that a retailer and manufacturer could collectively reach that would serve to harm competition and violate antitrust laws. One rather troublesome example is an agreement between a single manufacturer and a single retailer to fix retail prices.<sup>78</sup> More problematic are potential agreements between a single Category Captain and multiple retailers to fix retail prices.<sup>79</sup> The discussion in Part II.A.1 illustrates both problems.<sup>80</sup>

While antitrust laws prohibit most price fixing, the mere discussion of price between retailer and manufacturer requires further consideration. As discussed, retail pricing is one of the main components of category management decision-making. Therefore, in a vertical relationship between manufacturer and retailer<sup>81</sup> it may be acceptable for a Category Captain to analyze the category and proffer objective price recommendations to the retailer.<sup>82</sup> A retailer is then at liberty to

78. This practice is known as vertical resale price maintenance.

79. This would result in a combination of a vertical resale price maintenance violation as well as a horizontal price-fixing facilitated by a horizontal agent. Furthermore, this would be more problematic because it could eliminate all competition in a given market and with the Captain monitoring prices produce a relatively stable cartel.

80. While it is clear that the complexities of any given situation could lead to either a Section 1 or a Section 2 violation, this Part concentrates on Section 1 violations for purpose of analysis.

81. Often times a retailer maintains a private-label product that competes directly with a Category Captain's branded product. *See Steiner, supra* note 11, at 79. While never definitively decided by the courts, it seems that in all but the most rare situations the relationship would be considered vertical. If, for instance, the manufacturer's product and the retailer's private label were the only two in the category, the relationship would be horizontal and any Category Plan to agree on prices would be per se illegal. *See United States v. Trenton Potteries Co.*, 273 U.S. 392 (1927); *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940); *Arizona v. Maricopa County Med. Soc'y*, 457 U.S. 332 (1982). For a discussion on differentiating between a horizontal and a vertical relationship, *see E. THOMAS SULLIVAN & HERBERT HOVENKAMP, ANTITRUST LAW, POLICY AND PROCEDURE* 490-91 (4th ed. 1999). Furthermore, the Supreme Court touched upon the vertical-horizontal distinction, in a rather clear-cut case of a manufacturer that sold its products both to wholesalers and retailers. *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305 (1956). For the purposes of this Note, a vertical relationship is assumed.

82. The Category Captain may also pay a fee for this privilege. *See Merrefield, supra* note 26. For a discussion on why this may be problematic, see Parts II.C and III.A.

use, reject, or alter those recommendations as it sees fit.<sup>83</sup> Once the retailer determines its retail prices, either party may perform the work necessary to implement the category plan. If a manufacturer does no more than suggest that a retailer charge a given price, similar to printing a Manufacturer Suggested Retail Price directly on a product label, there is not likely liability under Section 1 of the Sherman Act.<sup>84</sup>

Nevertheless, as described by at least some large retailers the Category Captain relationship is one that is inherently collaborative.<sup>85</sup> As such, the relationship opens the door for agreements to maintain a minimum or a maximum resale price. Each scenario yields different antitrust consequences, presented below.

### 1. Minimum Resale Price Maintenance

In situations where a manufacturer does not have a monopoly in a given product category,<sup>86</sup> it may find itself subject to the influence of a large retailer or retailer cartel with equivalent market power.<sup>87</sup> In such a situation, the individual retailer or cartel may leverage its clout

83. According to Ed Gallina, Executive Director of Category Management for Associated Wholesale Grocers, “[w]hen you let the category captain run the [category management] plan, there’s a problem. . . . Retailers have to get information from their vendors and then write their category management plan themselves.” *Are Captains Antitrust-Worthy?*, SUPERMARKET NEWS, June 9, 2003, at 18.

84. *See generally* United States v. Colgate & Co., 250 U.S. 300 (1919). Under the Colgate Doctrine, a manufacturer may announce a Manufacturer Suggested Retail Price (“MSRP”) to the retailer without taking any further action to influence the retailer to sell at that price. Any action by which the manufacturer seeks to obtain the retailers agreement to adhere to a resale price, however, yields concerted action, and thus triggers the watchful eye of the Sherman Act. This distinction is easily explained by Section 1’s requirement of concerted action. *Id.* However, the courts have not clarified the line between acceptable and unacceptable behavior. For instance, a manufacturer may condition its service or promotional funding on compliance with a specific resale price. *See* *Acquire v. Canada Dry Bottling Co. of New York*, 24 F.3d 401 (2d Cir. 1994). *But see* *Bender v. Southland Corp.*, 749 F.2d 1205 (6th Cir. 1984), in which a manufacturer recommended, but did not mandate, resale prices as part of a franchise agreement. The manufacturer closely monitored the prices, requiring reporting even when prices remained stable. The court ruled that this might have been sufficient to violate Section 1. *Id.*

85. Kevin Hade, Vice-President of Category Management for Ukrop Supermarkets, describes the relationship as one in which the Captain works with the retailer and potentially other manufacturers, all to make collaborative category management decisions. *FTC Slotting Day 2*, *supra* note 1, at 325–26.

86. Where the manufacturer has monopoly power in a given product category it is likely to seek a maximum resale price to obtain the most consumer surplus possible, rather than a minimum price. *See* Steiner, *supra* note 11, at 79; *see also infra* Part III.A.2.

87. The recent surge in market concentration has yielded considerable market power in the grocery segment. *See supra* note 1. For an example of a large retailer leveraging its scale to coerce anticompetitive conduct from—in this case multiple,—manufacturers, see *Toys “R” US, Inc. v. FTC*, 221 F.3d 928 (7th Cir. 2000).

to influence the manufacturer to maintain minimum resale prices at competing retailers. In doing so, the retailer or cartel coerces the manufacturer to sell its products to other retailers only on the condition that the retailer does not resell the product for less than an agreed to price.<sup>88</sup> This conduct, known as vertical minimum resale price maintenance,<sup>89</sup> is a per se violation of Section 1 of the Sherman Act.<sup>90</sup>

In 1911, the Supreme Court for the first time ruled that any agreement to enforce a minimum resale price is a per se violation of Section 1 of the Sherman Act.<sup>91</sup> While minimum resale price maintenance is an old practice, its seminal case, *Dr. Miles Medical Company v. John D. Park & Sons Co.*,<sup>92</sup> still provides an excellent illustration of the risks of anticompetitive behavior that may result from retailer market power and compliant manufacturers.<sup>93</sup>

In fact, the market conditions leading to *Dr. Miles* resemble those currently emerging in the grocery industry.<sup>94</sup> *Dr. Miles* was a medicine manufacturer<sup>95</sup> that was by its own account quite concerned

88. While it may seem that a manufacturer would impose minimum resale price maintenance, retailers have been shown to do so as well. See HERBERT HOVENKAMP, ENTERPRISE AND AMERICAN LAW 1836–1937, at 341 (1991). A manufacturer could attempt to maintain a minimum resale price in several ways. On the one hand, it could do so explicitly, as discussed in this Part. On the other hand, the Category Captain could offer inflated price recommendations to all of its retailers and hope that they would not realize that the recommendations were inflated. As discussed, *infra* Part III.B, this has at least some chance for success.

89. Vertical simply refers to the fact that the manufacturer and retailer exist at different stages of the supply chain. Price maintenance, as the name implies, is an agreement to set or fix prices at an agreed to level. Resale indicates the requirement that the agreement have to do with the initial purchaser's reselling of the good.

90. 324 Liquor Corp. v. Duffy, 479 U.S. 335, 341–43 (1987).

91. *Dr. Miles Med. Co. v. John D. Park & Sons Co.*, 220 U.S. 373, 408–09 (1911). Although the fact pattern in *Dr. Miles* presented only minimum resale price maintenance, the Court's opinion appears to have placed a per se restriction on all resale price maintenance. The court later confirmed this by so holding in *Albrecht v. Herald Co.*, 390 U.S. 145 (1968), a case involving maximum resale price maintenance. It was not until 1997 that the Court decided that maximum resale price maintenance was subject only to Rule of Reason analysis, thus overruling *Albrecht*, but leaving *Dr. Miles* intact. *State Oil Co. v. Khan*, 522 U.S. 3 (1997); see *infra* Part III.A.2.

92. 220 U.S. at 373.

93. Congress's initial reaction was to legislate around the result in *Dr. Miles* by passing the Miller-Tydings Act, ch. 690, tit. 8, 50 Stat. 673, 693 (1937), authorizing states to permit resale price maintenance. However, in 1975 Congress repealed the Miller-Tydings Act by passing the Consumer Goods Pricing Act of 1975, Pub. L. No. 94-145, 89 Stat. 801, returning *Dr. Miles* to the much deserved status of controlling precedent.

94. As discussed in this Part, at the time of *Dr. Miles*, chain grocery stores were emerging as a market force. Market power was in the hands of independent wholesalers and retailers acting as cartels. Today, market power is in the hands of individual firms that do not need cartel agreements to wield their power.

95. *Dr. Miles*, 220 U.S. at 374.

with protecting its independent non-chain customers along with its own good will and reputation.<sup>96</sup> Miles operated in a business environment in which a group of retailers acting as a cartel threatened to boycott manufacturers that did not grant them favorable terms.<sup>97</sup>

Faced with an onslaught of pressure from new chain store competitors, the National Wholesale Druggists' Association ("NWDA") and the National Association of Retail Druggists ("NARD"), trade associations acting as a cartel,<sup>98</sup> exerted considerable leverage over drug manufacturers to maintain minimum resale prices.<sup>99</sup> As part of their efforts, the NWDA and NARD members agreed to coerce their suppliers to demand that their resellers charged purchasers a minimum price.<sup>100</sup> The NWDA and NARD would then threaten to boycott the manufacturer if it did not concede.<sup>101</sup>

To facilitate this, the retail druggists also regularly shared lists of retailers that undercut the price scheme.<sup>102</sup> As such, although it was not itself part of the cartel seeking minimum resale prices,<sup>103</sup> Dr. Miles

96. *Id.* at 374–75 (noting that “[Dr. Miles] alleged that most of its sales were made through retail druggists and that the demand for its remedies largely depended upon their good will and commendation, and their ability to realize a fair profit”).

97. HOVENKAMP, *supra* note 88, at 341. The favorable terms coerced were somewhat different than one might expect. Unlike today where single giant firms may demand a price concession, the retailers at the time of *Dr. Miles* joined together and coerced manufacturers to maintain minimum resale prices. This collusion enabled small retailers to compete with larger retailers despite having higher costs. *Id.*

98. *Id.* at 341–42, 344–45. NARD was a trade association composed of independent drug retailers accounting for 90 percent of retail druggists. *Id.* at 345. NWDA was a trade association composed of 95 percent of wholesale druggists. *Id.*

99. *Id.* at 341–42.

100. *Id.* at 341.

101. *Id.*

102. *Id.* at 345. Nevertheless, there were also countervailing interests; large discounters were leveraging their massive buying power to induce manufacturers to give discounts greater than what was justified by cost savings in filling such a large order. 79 CONG. REC. 9077 (1935), reprinted in 4 THE LEGISLATIVE HISTORY OF THE FEDERAL ANTITRUST LAWS AND RELATED STATUTES 2930–31 (Earl W. Kintner ed., 1980) [hereinafter ANTITRUST HISTORY].

103. A cartel composed of manufacturers did in fact exist and colluded with NARD and NWDA. See *Jayne v. Loder*, 149 F. 21, 23–24, 27 (3d Cir. 1906). It is not clear whether Dr. Miles was a member of this cartel, as no mention is made in the case. Nevertheless, it appears quite clear that it was the NWDA that exerted the pressure for manufacturers to maintain such a plan. See *John D. Park & Sons Co. v. Nat'l Wholesale Druggists' Ass'n*, 67 N.E. 136, 137 (N.Y. Ct. App. 1903).

At a meeting of [NWDA] a plan was devised and adopted for the conduct of the business of the sale of proprietary goods, which was in the form of a petition addressed to the proprietors, asking them to fix a uniform jobbing price for fixed quantities, and also a selling price by the druggists, which they were to agree to maintain, and that the druggists should be allowed the difference between the jobbing and the selling price as their profit or rebate, which they asked should be not less than 10 per cent; the proprietors defraying the expenses of boxing and freight to the nearest transportation station of the buyer.

was subject to the considerable influence of the druggist cartel. Therefore, Dr. Miles had a vested interest in inducing a minimum retail price from its non-cartel retailers.

In response, Dr. Miles attempted to control the sale and marketing of its medicine by mandating retailers sell at a price high enough for independents to compete.<sup>104</sup> Specifically, Dr. Miles sold its medicine pursuant to two different contracts—the first a wholesale consignment contract<sup>105</sup> and the second a retail agency contract<sup>106</sup>—both of which were designed to control prices long after Dr. Miles relinquished title.<sup>107</sup> The consignment contract purported to make retailers “[w]holesale distributing agents.”<sup>108</sup> Under the terms of the agreement, medicine was invoiced to the consignee at a price that matched the minimum price at which the medicine could then be resold. The agents simply earned a commission on the invoice price. Furthermore, the consignee was required to agree to sell only to Dr. Miles’s “designated retail agents,” and to return all unsold medicine on demand.<sup>109</sup>

Likewise, the retail agency contract also contained terms designed to maintain a minimum resale price. Specifically, its terms prevented retailers from selling at a price below that printed on the medicine itself. Furthermore, its terms also prohibited sellers from giving quantity discounts and from selling to any wholesaler or retailer not accredited by Dr. Miles.<sup>110</sup>

Prior to *Dr. Miles*, courts took the position that a manufacturer’s attempt to fix retail prices was illegal only to the extent that it facilitated collusion amongst retailers.<sup>111</sup> The pre-*Miles* theory was that if one manufacturer set minimum retail prices with a single retailer, then other retailers would still remain to price-compete.<sup>112</sup> The other

*Id.* Moreover, “[a] manufacturer would ordinarily prefer *not* to deal with colluding retailers, because the higher markup by retailers reduce[s] the demand for the manufacturer’s product.” HOVENKAMP, *supra* note 88, at 344 (emphasis added). But for the price floor, many of the smaller druggist could not have made a profit or competed with larger chains. *See Nat’l Wholesale Druggists’ Ass’n*, 175 N.Y. at 137. On the other hand, Dr. Miles could have presumably continued selling to the larger retailers long after the smaller druggists failed.

104. *See Dr. Miles*, 220 U.S. at 374–75.

105. *Id.* at 394.

106. *Id.*

107. *Id.*

108. *Id.* at 395–96.

109. *Id.* at 396.

110. *Id.* at 398–99.

111. *See, e.g., John D. Park & Sons Co. v. Hartman*, 153 F. 24, 42–46 (6th Cir. 1907).

112. *See HOVENKAMP, supra* note 88, at 343.

retailers acting competitively would provide downward pressure on price, thus making the agreement between a single retailer and a single manufacturer less problematic from an antitrust perspective. *Dr. Miles*, however, eliminated this breathing room in the law of vertical restraints, making *all* instances of vertical minimum resale prices a per se violation of Section 1 of the Sherman Act.<sup>113</sup> Therefore, after *Dr. Miles* the existence of potential competing retailers is irrelevant.

Despite several temporarily successful attempts to legislate around *Dr. Miles*, it remains good law.<sup>114</sup> The practical effect of *Dr. Miles* has been that *any* agreement between buyer and seller to maintain a minimum resale price is illegal. This, of course, precludes a defendant from arguing standard antitrust defenses such as lack of market power, lack of anticompetitive effects, or any pro-business justification for its actions. Therefore, any argument that maintaining a minimum resale price was positive for the manufacturer, its independent retailers, or consumers, did not factor into the *Dr. Miles* Court's calculus.

Although the Supreme Court has since abandoned its per se approach to maximum resale price maintenance<sup>115</sup> and other non-price vertical restraints in favor of the more lenient Rule of Reason,<sup>116</sup> the Court has maintained its stance that minimum resale price maintenance is a per se violation of Section 1 of the Sherman Act.<sup>117</sup> *Dr. Miles* was a unique case, but quite illustrative of the ease with which vertical minimum resale price fixing can arise. Because of the nature of the challenge and the parties involved, the Court properly<sup>118</sup> addressed *Dr. Miles* as an instance of vertical price fixing. As history shows, however, *Dr. Miles* was actually a case of independent retailers using their cartel influence to shield themselves from corporate chains' attempts to leverage their scale to induce lower prices from manufacturers.

113. *Dr. Miles*, 220 U.S. at 408–09.

114. *See supra* note 93.

115. *State Oil Co. v. Khan*, 522 U.S. 3 (1997). For a discussion, see *infra* Part III.A.2.

116. *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 47–59 (1977) (providing an excellent discussion of per-se treatment in antitrust law).

117. *See, e.g.*, *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 341–43 (1987).

118. This was the proper approach primarily because *Dr. Miles* was the plaintiff in the lawsuit in which it sued its reseller for not maintaining a contractually agreed-to price. It is easy to conceive of, however, a lawsuit in which NARD or NWDA is sued for its collusive behavior to fix prices as horizontal actors. *See, e.g.*, *Arizona v. Maricopa County Med. Soc'y*, 457 U.S. 332 (1982); *see also supra* note 81.

While *Dr. Miles* is an old case, the market conditions leading to the antitrust violations therein are far from stale. Considering the rapidly increasing market power possessed by today's grocers, it is quite possible that a retailer would wield its power to coerce a manufacturer Category Captain to help establish minimum resale prices amongst competing retailers.<sup>119</sup> A retailer with market power sufficient to influence a manufacturer may decide that it would benefit from establishing a price floor for a certain product. If the retailer acts alone to raise prices above a certain level in a market that it is not the only seller, a substantial number of consumers might purchase the product at a competing retailer. As such, the retailer may seek to have its competitors maintain a similar price floor for the targeted product.<sup>120</sup>

It is here that a manufacturer Category Captain may become useful.<sup>121</sup> A retailer may influence a Captain that also serves as Captain at a competing retailer<sup>122</sup> to recommend prices that are higher than market conditions justify. The retailer may do this on its own, or in collusion with one or more other retailers. For instance, a large retailer may attempt to sway its Category Captain to recommend supra-competitive prices to the retailer's competitors that the Captain also serves. Alternatively, as in *Dr. Miles*, retailers may act in collu-

119. Furthermore, there is evidence that a Category Captain would be successful in requesting a price increase from a retailer. In fact, in a paper presented to the Annual Meeting of the American Economic Association, Robert L. Steiner discusses encounters in his consulting practice in which he has learned of Category Captains who have successfully lobbied retailers to raise prices on their private label products to correspond with price increases on the captain's branded product. Steiner, *supra* note 51, at 23. With manufacturers and retailers working hand-in-hand to maintain price gaps in their own competing products within that single chain, it does not require a huge leap of faith to imagine an expansion of this conduct to include a competing chain.

120. Generally speaking, most manufacturers of products in a competitive market want to keep prices low to increase profits. Nevertheless, the Market Power School of antitrust analysis contends that the retailer acts as a "gatekeeper," controlling the extent and terms of a manufacturer's access to consumers. Edward C. LaRose & Patrick J. Poff, *Slotting Allowances and the Emerging Antitrust Enforcement Debate*, 74-Nov. FLA. B.J. 42, 43 (2000), available at <http://www.flabar.org/>. In fact, according an executive at Wal-Mart, "in time . . . you will see only two offerings per category on the shelf—the national brand leader and the store brand. There will be no space available for the second or third brand player in the category." Steiner, *supra* note 51, at 10. This access to consumers may present a manufacturer Captain with a choice of complying, or losing its favorable position at the powerful retailer. When one considers this in light of the use of slotting fees as a barrier to entry with the potential to limit consumer choice, red flags go up. See, e.g., Gallun, *supra* note 64, at 17.

121. This is not to say that the retailers could not fix prices without the aid of the Captain. Certainly retailers can eliminate the middleman and fix prices all on their own.

122. A single manufacturer may serve as Captain at many large retailers. For instance, Del Monte claims that it serves as Category Captain at almost all of the top twenty-five retailers and wholesalers, nationwide, for relevant categories. See Urbanski, *supra* note 5, at S10.

sion to persuade the Category Captain to recommend supra-competitive prices to non-participating retailers. In whatever shape or form the collusion should arise, a challenge should result in a per se violation of Section 1 of the Sherman Act.

## 2. Maximum Resale Price Maintenance

It is fair to say that in a typical product market a manufacturer has an incentive to keep resale prices as low as possible in order to maximize throughput and thereby maximize profits.<sup>123</sup> Accordingly, it may be most appropriate to view vertical minimum resale price maintenance as driven by retailers. In a situation where a *manufacturer* that has market power sells to retailers with their own market power, however, the manufacturer may seek to enforce a *maximum* resale price in order to prevent the retailer from exploiting its own market power to the manufacturer's detriment.<sup>124</sup> Unlike vertical minimum resale price maintenance agreements, the Court has held that vertical maximum resale price maintenance agreements must only survive a Rule of Reason analysis for a party to avoid liability under Section 1 of the Sherman Act.<sup>125</sup>

123. In a competitive product market, a manufacturer will maximize profits by selling the most goods it possibly can. This is because, in a competitive market the firm is a "price taker," selling at whatever price the market will bear. Any increase in price will cause consumers to substitute away to a different product. See HOVENKAMP, *supra* note 42, at §1.1b. Nevertheless, markets are rarely perfectly competitive, and in the world of consumer products retailers and manufacturers battle for their share of consumer surplus. See *id.*; see, e.g., Steiner, *supra* note 11, at 79–80.

124. This fact enables the manufacturer to keep for itself the majority of a consumer surplus, while leaving little to the retailer. Without manufacturer-imposed maximum prices, a retailer with market power can sell at a higher price, thus reducing the total volume of product sold, and a reduction in corresponding profit to the manufacturer. See Peter Carstensen & David Hart, *Khaning the Court: How the Antitrust Establishment Obtained an Advisory Opinion Legalizing "Maximum" Price Fixing*, 34 U. TOL. L. REV. 241, 257 (2003). *State Oil Co. v. Khan* involved a gasoline producer that mandated that its retailers sell for only 3.5 cents above wholesale price. 522 U.S. 3, 7–8 (1997). The retailer was free to sell at a higher price, but was contractually obligated to remit all revenue gained from the higher prices back to the producer. *Id.* at 8. The Supreme Court ruled that the vertical maximum resale price maintenance agreements are subject to Rule of Reason analysis. *Id.* at 18, 22. Carstensen & Hart, *supra*, at 259–65, argue that the Supreme Court erred in its *Khan* conclusion, because *Khan* should not have been viewed as an independent business, but rather more like a junior partner in partnership with State Oil (or an employee or agent of State Oil), and, as such, the case should not have raised antitrust concerns.

125. *Khan*, 220 U.S. at 22. By insisting on applying Rule of Reason analysis, the Court overruled its 1968 decision in *Albrecht v. Herald*. *Id.* Under Rule of Reason analysis the Court will look at the actual effects of the challenged restraint upon competition: price, quantity, and consumer choice. Specifically, the court must determine whether the challenged agreement "is such as may suppress or even destroy competition. . . . [T]he court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable." Chicago Bd.

In *State Oil Co. v. Khan*,<sup>126</sup> the Court held that vertical maximum resale price maintenance is generally beneficial to consumers and that Rule of Reason analysis would uncover and punish those instances of maximum price setting that actually produced anticompetitive effects.<sup>127</sup> This leniency in most instances permits a Category Captain to urge or even coerce a maximum resale price for its products. In fact, under current doctrine there are few, if any,<sup>128</sup> examples of vertical maximum resale price maintenance that would violate Section 1 of the Sherman Act. One such example, however unlikely, would be the scenario where a manufacturer and retailer collude to maintain a maximum resale price below marginal cost<sup>129</sup> for the purpose of erecting a barrier to entry or to drive competition from the market.<sup>130</sup>

A competitor may sometimes engage in below cost predatory pricing in order to secure a monopoly in the market and later raise prices to monopoly level.<sup>131</sup> Predatory pricing not only can be used as a means to eliminate a competitor unable to sustain a loss, but also to discipline a fellow cartel member that has chosen to cut prices.<sup>132</sup>

### B. *Sherman Act Section 2*

Section 2 of the Sherman Act makes it an offense for a firm to monopolize or attempt to monopolize trade or commerce.<sup>133</sup> In a

of Trade v. United States, 246 U.S. 231, 238 (1918). Put differently, traditional Rule of Reason analysis asks: “(1) What is the specific restraint at issue? (2) What are its likely anticompetitive effects? (3) Are there offsetting procompetitive justifications? (4) Do the parties have sufficient market power to make a difference?” *California Dental Ass’n v. FTC*, 526 U.S. 756, 782 (1999) (Breyer, J., dissenting).

126. 522 U.S. at 3.

127. *Id.* at 15–17.

128. One such scenario would be a manufacturer holding a monopoly in a certain good imposing a maximum resale price on a relatively powerless reseller. *See, e.g., Khan*, 522 U.S. 3. Despite the outcome in *Khan*, Carstensen & Hart, *supra* note 124, at 259–65, argue that *Khan* was not, in fact, such a scenario. Even if this view is correct, the Supreme Court’s decision is binding.

129. In proper formulation prices cannot be set below an “appropriate measure” of costs, and result in an antitrust violation when the price-cutter has a dangerous probability of recovering its investment in the below cost pricing by later charging a higher price. *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 222–24 (1993).

130. Predatory pricing, when attempted, may be analyzed under either Section 1 or Section 2 of the Sherman Act. *See Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 326, 338 (1990).

131. *Brooke Group*, 509 U.S. at 224.

132. *See generally id.* at 225.

133. 15 U.S.C. § 2 (2000).

competitive market, firms may seek to eliminate their competitors.<sup>134</sup> Accordingly, turning over the keys to a retail chain's category management decisions to a single manufacturer, thus limiting input from other manufacturers, could lead to numerous violations under Section 2 of the Sherman Act. The most obvious opportunities include a Category Captain that acts to mislead a retailer by offering less than accurate data regarding optimal product assortment, placement, pricing, or promotion;<sup>135</sup> and a malicious Category Captain that acts to sabotage the in-store product or promotional materials of competitors, thus deciding to forego competition on the merits.<sup>136</sup>

In a perfect world, firms and their employees are honest and compete solely on the merits of their product(s) or service(s) and antitrust laws are unnecessary. Nevertheless, corporations such as Enron,<sup>137</sup> WorldCom,<sup>138</sup> and Arthur Andersen<sup>139</sup> have adequately demonstrated that corporations and their employees are all too willing to exhibit behavior that far exceeds the outer boundaries of legality and acceptable business ethics.<sup>140</sup> In the shadow of these scandalous undertakings all but the most heinous abuses of a Category Captaincy may pass unchallenged or even unrecognized.<sup>141</sup>

134. The competitive market allows for each player to seek monopoly profits through legitimate competitive means. It is only when a firm seeks to gain or maintain monopoly power through anticompetitive means that antitrust becomes concerned. See generally HOVENKAMP, *supra* note 42, at § 1.3. Furthermore, a firm that is the sole supplier of a good necessarily receives one-hundred percent of the revenues generated in that market. This is necessarily greater than the share should a competitor exist. As such, a manufacturer has a rational incentive to eliminate its competitors. This, of course, assumes that businesses are not motivated by any potential disutility experienced by a competitor that it eliminates.

135. See, e.g., *Conwood Co., L.P. v. United States Tobacco Co.*, 290 F.3d 768 (6th Cir. 2002).

136. *Id.*

137. In 2002, Enron corporate officials were suspected of or charged with a myriad of violations of the law and public trust. A brief list includes: securities fraud, illegal kickbacks, tax law violations, fraud, and surreptitious dealings to manipulate stock price. Peter Behr & Carrie Johnson, *U.S. Plans To Seek New Enron Charges: Accounting Officer, CFO's Wife Targeted*, WASH. POST, Feb. 1, 2003, at E01, available at <http://www.washingtonpost.com/ac2/wp-dyn?pagename=article&node=&contentId=A8872-2003Jan31>.

138. In 2002, as part of an accounting scandal, Worldcom filed for the largest (at the time of this writing) bankruptcy in U.S. history, seeking forgiveness of \$36 billion in debt. Rebecca Blumenstein & Shawn Young, *WorldCom Creditors Back Plan To Reorganize in Bankruptcy*, WALL ST. J., Apr. 14, 2003, at A1.

139. Arthur Andersen served as Enron's accounting firm and went so far as to shred documents to avoid legal consequences. See Ken Brown, *When Enron Auditors Were on a Tear*, WALL ST. J., Mar. 21, 2002, at C01.

140. Furthermore, a reading of the literature seems to indicate that many lower level employees simply followed orders without questioning the legality of the business directives they had been issued.

141. For instance, in *Conwood Co., L.P. v. United States Tobacco Co.*, the perpetrating corporation was able to get away with serious anticompetitive acts before suit was filed. 290 F.3d 768 (2003).

Retailers often stress that it is necessary for a Category Captain to be trustworthy, because the retailer would otherwise sever the relationship.<sup>142</sup> This, however, is nothing more than rhetoric.<sup>143</sup> Certainly if a Category Captain is completely honest and approaches its work with only the retailer's best interests in mind then the retailer would be more than justified in relying on the Category Captain. As discussed in this Part, however, such a presumption on the part of a retailer may not be safe or even rational. It seems that if a retailer were ultimately concerned about perfect accuracy in its Category Management activities the rational decision would be to staff the work itself<sup>144</sup> and make up the additional costs by carrying only profitable brands.<sup>145</sup> At that point, a manufacturer could eliminate many of the in-house costs associated with Category Management endeavors and pass these savings on to its retailers in the form of lower priced products.<sup>146</sup> The retailer could use the savings from lower-priced products to invest in Category Management programs of their own.<sup>147</sup> Maybe most importantly, however, the retailer could eliminate all risk of malfeasance on the part of a Category Captain.

But the world of merchandising and retail decision-making is often a game played at the margins. A good deal of Category Management is based upon data that can be interpreted in a myriad of different ways.<sup>148</sup> Most Category Captains are likely too sophisticated to tell a retailer that a top-selling brand of deodorant should be moved to the bottom shelf or that a retailer's private label product should be discontinued all together, and most retailers are likely too

142. *Id.* at 775. In *Conwood*, a retailer asserted that the surest way for a Category Captain to be shown the door would be to mislead the retailer. *Id.*

143. There was no evidence that any retailer ever removed the offending Category Captain from its duties and privileges. *See generally Conwood*, 290 F.3d at 768.

144. Retailers achieve this either internally, or through an external third party.

145. At minimum, the retailer could seek an outside, disinterested third party to aid in decision-making.

146. With the current state of market power at the retailer level, they could almost certainly negotiate a favorable price. By example, Wal-Mart leverages its scale to receive the best possible price by threatening to stop carrying all or part of a manufacturer's products. *See Borghesani, Jr. et al., supra* note 1, at 50.

147. Smaller manufacturers that do not likely receive the Category Captaincy opportunities would also be entitled to receive the lowered prices, as mandated by the Robinson-Patman Act. To ensure that the retailer actually performs the Category Management work, the manufacturer could offer rebates on proportionally equal terms to all retailers.

148. *See, e.g., Conwood*, 290 F.3d at 776. USTC provided "skewed" data that stressed national figures instead of more relevant local figures to some of its retailers. *Id.*

intelligent to fall into this type of trap.<sup>149</sup> Nevertheless, there is a strong disincentive for a manufacturer to spend its money on Category Management research and labor to then recommend that its *own* brand be moved out of the store or relegated to the bottom shelf only to be replaced by a competing product.<sup>150</sup> This coupled with the fact that at least some retailers allow their Category Captain to make all relevant category decisions,<sup>151</sup> creates a situation with both incentive and opportunity for the Category Captain to take advantage of the relationship.

A Category Captain could easily recommend that a single, less significant competing product disappear,<sup>152</sup> or that the retailer carry one of the manufacturer's solid but slower moving products or brands.<sup>153</sup> The Captain might also suggest that its own slower moving brand receive better shelving and promotion than would be optimal for the store.<sup>154</sup>

While it may seem unthinkable for a manufacturer to breach a retailer's trust,<sup>155</sup> the incentive to do so can be significant. The United States Tobacco Company ("USTC") was America's leading producer

149. See Albert A. Foer, *Divestiture and the Category Captain: New Considerations in Merger Remedies*, <http://www.antitrustinstitute.org/recent/153.cfm> (Nov. 19, 2001). However, in *Conwood*, retailers either fell for or abided by deceptive practices by the Category Captain. 290 F.3d at 768.

150. The most rational incentive for a manufacturer is to serve as Category Captain for those retailers where the manufacturer's products are receiving less than optimal distribution, shelf placement, pricing, or promotion. Otherwise, the manufacturer is better off not spending resources and free-riding. The question is, really, whether Manufacturer A would elect to serve, if chosen, as Category Captain, in a store where its product was "second best" from the store's perspective and where that product was appropriately placed. Theoretically, a manufacturer has no incentive other than to make certain a second manufacturer does not provide misleading category information to the retailer, and to improve the efficiency of the overall category. The only rational reason for a manufacturer, then, not to cede a Category Captaincy opportunity to a second manufacturer is fear that the Category Captain system is, indeed, flawed, and that the second manufacturer will mislead the retailer. This, of course, assumes that the first manufacturer is honest and will not attempt to provide its product supra-competitive placement, price, assortment, or promotion.

151. See *supra* note 59.

152. The manufacturer would make this recommendation because it deems the product to be a competitive threat in the longer term. This would reduce competition and harm price-conscious consumers.

153. See, e.g., *Conwood*, 290 F.3d at 786.

154. *Id.* This would likely increase volume for that brand, justifying the decision, but could reduce overall volume for the category. Even if it merely hurts a competitive product, the deceptive manufacturer benefits. See *supra* note 28.

155. It may be dubious to refer to this as a relationship of trust in situations where the manufacturer has actually paid money for the "privilege" of serving as Category Captain. See *supra* note 26.

of moist snuff tobacco,<sup>156</sup> and controlled 77 percent of the relevant product market.<sup>157</sup> Conwood was one of only four competing firms in the market.<sup>158</sup> In a series of deceptive and malicious abuses of its Category Captain responsibilities, a capacity in which it served a significant number of retailers, USTC took affirmative steps to eliminate its competitors.<sup>159</sup> Specifically, USTC took advantage of its Category Captain relationship by providing misleading and false Category Management information and by making it difficult for consumers to locate competing brands at stores.<sup>160</sup>

The benefits to USTC were tremendous. USTC enjoyed the highest profit margin of any public company in America at the time of the court's decision, having raised its price an average of eight to ten percent per year every year between 1979 and 1998.<sup>161</sup> Recognizing that its near-monopoly profits would likely induce others to enter the market,<sup>162</sup> USTC erected barriers to entry and sought to eliminate that competition that already existed. It achieved this by leveraging its influence as Category Captain in a way that harmed competition and ultimately consumers.

USTC's first step was simply to convince stores to agree to use exclusively USTC display racks.<sup>163</sup> But from these humble beginnings, USTC's relentless pursuit of market share and entry barriers often

156. *Conwood*, 290 F.3d at 774. Ironically, Conwood and U.S. Tobacco were both created when a judicial decree broke up its parent, Duke Trust. *Id.* at 773.

157. *Id.* at 774. At the time of litigation, Conwood controlled thirteen and one half percent of the relevant market. *Id.*

158. *Id.*

159. *Id.* at 776–78, 787. USTC's own internal documents indicated that it sought “[to] continue with [a] Category Management action plan to eliminate competitive products,” “to limit the growth of the price value market segment,” to “inhibit competitive growth,” and to “cut[] . . . distribution of competitive brands.” *Id.* at 776, 777, 778. In fact, USTC's Chairman testified that his company had pursued a “strategy of eliminating competitive distribution.” *Id.* at 787.

160. *Id.* at 777–80. USTC removed competitors' in store racks and placed competing product in USTC racks, making it difficult for customers to locate non-USTC snuff. *Id.* at 778.

161. *Id.* at 774. USTC achieved this despite losing market share at a rate of approximately 1 percent per year between 1979 and 1998. *Id.*

162. *See id.* Despite these high profits, the *Conwood* court reported that no firm had entered the market since 1990. *Id.*

163. *Id.* at 775. An exclusive display rack means that the moist snuff of all competing manufacturers was shelved in a unit created by a single manufacturer, in this case USTC. *Id.* at 775. Because of legal restrictions on tobacco advertising, in-store signage was particularly important for moist snuff—the display rack provides one of the more visible forms of in-store advertising. *Id.* at 774. In fact, a USTC competitor noted, “the point at which the buyer makes his purchase decision is the optimal time to convince the buyer to purchase a particular brand of moist snuff.” *Id.* Yet in some instances, it was actually the store, itself, which requested the exclusive rack. *Id.* at 775.

turned into activity that blatantly violated Section 2 of the Sherman Antitrust Act. Focused on a goal of eliminating competing products, including “price value products” that sold at half the price of its own products, USTC leveraged its position as Category Captain to abuse retailer trust.<sup>164</sup>

For instance, USTC provided its retailers with sales data skewed to the national market rather than more relevant local sales data.<sup>165</sup> This data presented national-level data in a way that masked local product movement.<sup>166</sup> The result was an inaccurate prediction of moist snuff sales at local stores that unduly favored USTC products.<sup>167</sup> Such a subtle misrepresentation of product data likely appeared perfectly legitimate to an untrained eye and may never have been detected. Nevertheless, USTC went one step further and provided *false* data, inflated to induce stores to stock a slower moving USTC moist snuff product and drop competitors’ better selling stock-keeping units (“SKUs”).<sup>168</sup> It even went so far as to inflate actual sales figures.<sup>169</sup>

Furthermore, USTC’s abuse of its Category Captain position did not end with attempts to mislead retailers into stocking USTC brands. Where the lower priced products did make it to the retail shelf, USTC took action to obscure them, such that interested consumers could not locate them on the store shelves.<sup>170</sup> To accomplish this, USTC sought to have competing products displayed in USTC labeled racks.<sup>171</sup> Furthermore, USTC frequently removed Conwood display racks and corresponding point-of-sale materials, going so far as to schedule store visits when protesting retailer employees were not

164. *Id.* at 775–76, 777 (noting one USTC employee’s observation that “[a]lthough [USTC] control[s] the merchandising and the POS placements, which will make the consumer awareness of the price differential difficult, some . . . shoppers are always looking for a bargain.”).

165. *Id.* at 776. Retailers based their decisions of which products to carry upon this false sales data. *Id.*

166. *Id.*

167. *Id.*

168. *Id.*; Mary W. Sullivan, *Slotting Allowances and the Market for New Products*, 40 J.L. & ECON. 461, 464 (1997). SKU is short for Stock-Keeping Unit. “An SKU uniquely identifies each product by supplier, brand, size, flavor, and package type. An example of an SKU is Coca-Cola’s caffeine-free Tab in 2-liter bottles.” *Id.*

169. *Conwood*, 290 F.3d at 776.

170. *Id.* at 779 (noting that USTC employees “would remove Conwood racks and put Conwood’s products in USTC racks” and “would remove competitors’ racks and bag up their fresh product and place them under a counter”).

171. *Id.* at 778 (quoting a USTC salesperson that quipped “[e]ven though Conwood does not like the fact that we sometimes house the product in [USTC] vending . . . I feel it is better for them to be lost in our vending”).

working.<sup>172</sup> At times, USTC personnel even destroyed Conwood display racks.<sup>173</sup> Finally, USTC entered into exclusive dealing arrangements with retailers, which served to bolster the effects of its abuses of its Category Captain privileges.<sup>174</sup>

When one considers the sheer volume of SKUs a large retailer faces, it is not difficult to imagine how USTC could get away with such activities. In the category of moist snuff,<sup>175</sup> not even Wal-Mart has any personnel exclusively dedicated to its management.<sup>176</sup>

While USTC's actions are shocking, they are far from unique.<sup>177</sup> USTC did far more than merely walk the sometimes gray line of anti-trust violation. What is telling is the sheer effort that USTC exuded to exclude its competitors from the market, not by producing a product preferential to consumers, but by eliminating consumer choice. The *Conwood* case illustrates that retailers trust the top producer in a category to provide accurate information.<sup>178</sup> While this trust may be necessary for a continued working relationship, *Conwood* also provides warning that manufacturers may be willing to abuse the relationship at the expense to competing manufacturers, consumers, and even the retailer.

Moreover, it does not appear as though it were difficult for USTC to get away with its data manipulations; at least it does not appear that many retailers were willing to take action. It was not until one of USTC's competitors complained of abuses that litigation arose.<sup>179</sup> Robert Blattberg, Professor of Retailing at Northwestern University's Kellogg Graduate Business School, explained that few

172. *Id.* at 779 (recounting testimony from a convenience store clerk who "stated that when [she complained that a USTC salesman that removed Conwood display racks without store permission, he] would then come when she was not on duty and remove Conwood racks anyway").

173. *Id.* at 778.

174. *Id.* at 777 (discussing USTC's use of "exclusive vending rights" for the purpose of "control expanded competitive distribution and competitive POS").

175. Moist snuff accounted for a not so paltry \$1.68 billion in 1999. *Id.* at 774.

176. *Id.* at 776 (testimony of Robert Blattberg, a category management expert and professor at Northwestern's Kellogg Graduate Business School).

177. See, e.g., *FTC Slotting Day 2*, *supra* note 1, at 348-49. For instance, Pamela Mills, while working for a tortilla chip manufacturer, experienced a competitor that convinced a retailer to reduce shelf space for her tortilla chips, when that manufacturer's product had not previously been a proven winner at the store. See *id.* Similarly, Frito-Lay has been accused of paying for more shelf space than it needed to injure competitors. Borghesani, Jr. et al., *supra* note 1, at 57.

178. *Conwood*, 190 F.3d at 775.

179. The *Conwood* case does not expressly indicate what USTC action, specifically, precipitated the litigation. Given the subtlety of many of USTC's action, it was most likely the net effect of USTC's activities that led Conwood to file suit.

retailers have sufficient resources to dedicate to monitoring categories as small as moist snuff.<sup>180</sup> When viewed in light of the fact that retail Category Managers do not likely know as much as the manufacturer about the product category and its pricing and profitability,<sup>181</sup> it is not difficult to foresee a situation in which a manufacturer might stretch the truth to provide its product a favorable position at the retailer. Had USTC confined its misconduct to the misleading manipulation of data and the occasional misleading SKU recommendation, it would likely never have been caught. Moreover, the significance of such a transgression at a store chain with as much market throughput as Wal-Mart is substantial. While the billion-dollar settlement against USTC and the Supreme Court's denial of certiorari on the verdict<sup>182</sup> may give some Category Captains pause, the relationship's structure will continue to provide similar opportunities to other manufacturers.

Nevertheless, the level of control and influence that a Category Captain maintains at the retailer it serves lends itself to potential violations of both Sections 1 and 2 of the Sherman Act. The most likely violations of Section 1 involve attempts to maintain either maximum or resale prices. Furthermore, a disreputable manufacturer that affirmatively misleads a retailer or otherwise sabotages the in-store efforts of a competitor would very likely violate Section 2.

While it may be relatively easy to recognize decisions that may violate the Sherman Act, and therefore to avoid them, antitrust concerns may not always be so simple to avoid. Part IV of this Note explores the Robinson-Patman Act's price discrimination restriction and the related requirement that manufacturers provide their services to all retailers on proportionally equal terms. Part V will then provide recommendations for structuring Category Captain relationships such that firms might minimize antitrust concerns.

#### IV. IMPLICATIONS OF SECTION 2 OF THE ROBINSON-PATMAN ACT ON CATEGORY CAPTAINS

In the field of merchandise distribution a Goliath stands against divided forces plying a powerful weapon with a skillful hand against the vulnerable weaknesses of his opponents.

180. *Conwood*, 190 F.3d at 776.

181. *Id.*

182. *United States Tobacco Co. v. Conwood Co., L.P.*, 537 U.S. 1148 (2003).

The Goliath is the huge chain stores sapping the civic life of local communities with an absentee overlordship, draining off their earnings to his coffers, and reducing their independent business men to employees or to idleness.

His weapon is huge buying power, by the manipulation of which he threatens manufacturers and others with financial stringency or even bankruptcy if they refuse him the prices and terms he demands.

His opponents are not only these manufacturers, not only the independent competitors whom he seeks to eliminate, but the consuming public, whom he hopes to have at his mercy.

Their weaknesses, which he renders all the more vulnerable by playing off their strength against each other, are these:

First. The manufacturers' large overhead, which deepen their losses from business lost, and magnify their gains on new business gained.

Second. The decentralization of independent competitors, and the obstacles which the law raises against them if they attempt organized resistance to those manufacturers who seek to make up from them the net profits which they lose on the chains.

Third. The disorganized individualism and hand-to-mouth buying habits of the purchasing public, who cannot realize nor foresee—nor indeed, resist if they could—the merchandising tactics of the chains—practices which, because of their far-flung resources, they can concentrate with more deadly effect in one community at the cost of another.<sup>183</sup>

These are the words of Representative Wright Patman,<sup>184</sup> proffered to the House of Representatives on June 11, 1935 as part of his bill to amend Section 2 of the Clayton Act.<sup>185</sup> With a few minor augmentations, sparing the hyperbole, and adding to the mix larger manufacturers, one might mistake this for a present day Federal Trade Commission<sup>186</sup> report on the state of the grocery industry.

In the Pre-Robinson-Patman Act 1930s, independent grocers were seeing their business slowly erode to the coercive practices of rapidly emerging chain stores.<sup>187</sup> Specifically, large chains used their size to coerce quantity discounts above and beyond what was justified

183. ANTITRUST HISTORY, *supra* note 102, at 2927.

184. *Id.* at 2926. Although offered by Representative Patman in his name, the bill was actually written by former Department of Justice attorney H.B. Teegarden. *Id.* at 2933.

185. *Id.* at 2926.

186. The F.T.C.'s David Balto has expressed the commission's willingness to enforce the Act should a proper challenge be brought. *See FTC Slotting Day 2*, *supra* note 1, at 459–60.

187. As discussed in Part III.A.1, the independent sellers did not, themselves, react graciously.

by the actual economies of scale of order size.<sup>188</sup> Large corporate chains also coerced rebates from manufacturers, rationalized under the proposition that they were “advertising allowance[s]” or “brokerage” fees to cover the chain’s advertising costs.<sup>189</sup> As such, the Robinson-Patman amendment to the Clayton Act came into being explicitly as a means to allow all manufacturers, big or small, the opportunity to sell their goods free from retailer coercion, and to prevent the eventual monopolization of grocery business by large chains.<sup>190</sup>

At the time, chain stores accounted for one in every ten physical stores, and one in five dollars worth of merchandise sold.<sup>191</sup> Between 1926 and 1933 chain stores’ percentage of retail sales increased from 9 to 25 percent.<sup>192</sup> In terms of groceries, corporate grocery chains accounted for 52,514 stores,<sup>193</sup> while voluntary and cooperative chains operated approximately 53,000 stores.<sup>194</sup> Furthermore, manufacturers were not seen as being an evil from which consumers needed protection.<sup>195</sup>

Today, grocery retailers are again accumulating market power. Between 1987 and 2000 the market share controlled by the four largest grocery chains increased from 17.0 to 27.4 percent of the national market.<sup>196</sup> William H. Borghesani, Jr. and his colleagues at Keller and

188. See ANTITRUST HISTORY, *supra* note 102, at 2931.

189. *Id.* (noting that the small independent stores did not have the leverage to coerce in-kind payments).

190. *Id.* at 2930–31 (noting that large chains may offer consumers lower prices in the short run, but that once small competitors were driven out, higher prices and oppression would follow). In choosing to act before large chain stores’ power it got out of control, Congress may have learned its lesson from *Standard Oil*. *Standard Oil Co. of New Jersey v. United States*, 221 U.S. 1 (1911). *Standard Oil* was a large oil producer and a mammoth consumer of railroad freight. Because of the large amount of business it did, *Standard Oil* was able to coerce from its railroad freight suppliers a fifty percent rebate on its own freight, as well as fifty percent of the revenues that the railroads realized from *Standard Oil* competitors. WALTER ADAMS & JAMES W. BROCK, *THE BIGNESS COMPLEX: INDUSTRY, LABOR, AND GOVERNMENT IN THE AMERICAN ECONOMY* 137–39 (1986). *Standard Oil* provides an excellent example of what happens when Congress fails to act quickly to restore competitive market structures once they break down. See generally *id.* Similarly, in slightly more modern times the Supreme Court has espoused that Congress leveraged the Robinson-Patman Act to prohibit large firms from “securing a competitive advantage over a small buyer solely because of the large buyer’s quantity purchasing ability.” *FTC v. Morton Salt Co.*, 334 U.S. 37, 43 (1948).

191. ANTITRUST HISTORY, *supra* note 102, at 2958. This is, apparently, all retail, not just grocery.

192. JOSEPH CORNWALL PALAMOUNTAIN, JR., *THE POLITICS OF DISTRIBUTION* 7 (1955).

193. ANTITRUST HISTORY, *supra* note 102, at 2959. The top three corporate grocery chains account for approximately 24,000 stores. *Id.*

194. *Id.* A voluntary or cooperative chain was created when a number of independent stores group together as an independent merchants association in order to buy in quantity. *Id.* at 2934.

195. *Id.* at 2948.

196. See *supra* note 1.

Heckman have argued, however, that the appropriate measure of market power for American grocers is at a regional level, where market share of the four largest chains has risen from 49.3 percent in 1958 to 62.4 percent in 1987 in metropolitan areas with more than one million residents.<sup>197</sup> In contrast, economics Professors William Hildred and James Pinto assert that because consumers shop only in local economic markets, a proper analysis should focus on local concentration.<sup>198</sup> In fact, local market concentration often may be even higher than national figures.<sup>199</sup> For instance, in 1998 the four-firm market concentration was greater than 90 percent in the Buffalo-Niagara Falls market, while exceeding 73 percent in Hartford, 68 percent in Cleveland-Akron, and 66 percent in the Boston-Worcester-Lawrence market.<sup>200</sup>

While the current political climate is different than in Senator Patman's era, the economic factors made evident in his prose have returned to the forefront of American reality. As such, as mega-retailers begin to leverage their size, manufacturers may find themselves tempted to provide greater services with the products they sell<sup>201</sup> and, in doing so, violate the Robinson-Patman Act, as discussed in this Part.<sup>202</sup>

The Supreme Court has explained that Congress implemented the Robinson-Patman Act because Congress "considered it to be an evil that a large buyer could secure a competitive advantage over a small buyer solely because of the large buyer's quantity purchasing ability."<sup>203</sup> The injuries Robinson-Patman seeks to prevent include "the use of quantity price differentials [unrelated to] actual cost differences [in order to prevent such discounts from being used as] instruments of favor and privilege and weapons of competitive

197. Borghesani, Jr. et al., *supra* note 1, at 45-46.

198. William Hildred & James Pinto, *Impacts of Supply Chain Management on Competition 2* (Northern Arizona Univ. working paper, Apr. 2002), available at [http://www.cba.nau.edu/faculty/workingpapers/pdf/Hildred\\_2SCMonComp.pdf](http://www.cba.nau.edu/faculty/workingpapers/pdf/Hildred_2SCMonComp.pdf).

199. See Albert A. Foer, *Food Retailing: The Two Faces Of Supermarket Mergers*, <http://www.antitrustinstitute.org/recent/37.cfm> (Aug. 26, 1999).

200. *Id.* at n.9.

201. See, e.g., Nancy Griffin, *Polls Reveal Service Gaps Between Retailers and Suppliers*, SUPERMARKET NEWS, June 4, 2001, at 54, reproduced at [http://www.perishablesgroup.com/industry\\_articles/010604\\_pollsrevealgaps.html](http://www.perishablesgroup.com/industry_articles/010604_pollsrevealgaps.html). With the recent increase in market concentration, retailers have begun to demand more than just a good product. *Id.*

202. This carries a potential concomitant violation of Section 2(f) on the part of the retailer. 15 U.S.C. § 13(f) (2000).

203. *FTC v. Morton Salt Co.*, 334 U.S. 37, 43 (1948).

oppression.”<sup>204</sup> In short, the Act was implemented to prevent “large buyers [that] dominate a market in which many suppliers compete for sales [from] forc[ing] the suppliers to sell at such low prices as to prevent new buyers from entering the market.”<sup>205</sup>

As it reads today, Section 2(a) of the Robinson-Patman Act provides that “[i]t [is] unlawful for any [firm] to discriminate in price between different purchasers of commodities of like grade and quality.”<sup>206</sup> While price differentials are rather easy to spot, Congress was sophisticated enough to recognize that a manufacturer could charge all purchasers the same price, yet achieve price discrimination by offering valuable services and facilities to some purchasers and not others. As such, Section 2(e) of the Act prohibits a manufacturer from providing valuable services or facilities to purchasers unless such are offered to each purchaser on proportionally equal terms.<sup>207</sup> Finally, Congress recognized that it is sometimes the buyer that seeks the prohibited price differential. Therefore, Section 2(f) of the Robinson-Patman Act restricts buyers, here retailers, from knowingly receiving discriminatory prices.<sup>208</sup> As such, any attempt by a retailer to

204. *Id.* at 43–44 (quoting H.R. Rep. No. 74-2287, at 9 (1936)).

205. *Hoover Color Corp. v. Bayer Corp.*, 199 F.3d 160, 163 (4th Cir. 1999).

206. 15 U.S.C. § 13(a) (2000); *see* *FTC v. Anheuser-Busch, Inc.*, 363 U.S. 536, 550 (1960). Section 2(a) prohibits discrimination directly on price, a practice that is not directly tied to the Category Captain relationship and therefore not further explored in this Note.

207. 15 U.S.C. § 13(e) (2000). Section 2(e) provides that:

It shall be unlawful for any person to discriminate in favor of one purchaser against another purchaser or purchasers of a commodity bought for resale, with or without processing, by contracting to furnish or furnishing, or by contributing to the furnishing of, any services or facilities connected with the processing, handling, sale, or offering for sale of such commodity so purchased upon terms not accorded to all purchasers on proportionally equal terms.

*Id.* Furthermore, The Fred-Meyer Guides, found at 16 C.F.R. § 240 *et seq.* (2004), provide ample detail and examples as to the meaning of “proportionally equal” terms. *Id.* Essentially, a manufacturer may offer a certain amount of service or allowance for each dollar or unit sold, but may not have a logarithmically or exponentially expanding formula, such that bigger purchasers always receive better terms that are not justified from cost savings associated with such large orders. Section 2(e), along with Section 2(d), was designed to prohibit price discrimination in the form of advertising and promotional allowance. While 2(e) prohibits the manufacturer from directly “[f]urnishing services or facilities,” 2(d) prohibits a seller from “[p]ay[ing] for services or facilities.” *Id.* at §13(d); *see* *FTC v. Fred Meyer, Inc.*, 390 U.S. 341, 350–53 (1968); *George Huag Co. v. Rolls Royce Motor Cars, Inc.*, 148 F.3d 136 (2d Cir. 1998).

208. 15 U.S.C. § 13(f) (2000). Section 2(f) provides that “It shall be unlawful for any person engaged in commerce, in the course of such commerce, knowingly to induce or receive a discrimination in price which is prohibited by this section.” *Id.* While § 2(f) by its text applies only to price discrimination, case law has leveraged § 5 of the F.T.C. Act to apply Section 2(f) to violations of Sections 2(d) and 2(e). *Grand Union Co. v. FTC*, 300 F.2d 92 (2nd Cir. 1962). Section 2(d) makes it illegal for manufacturers to pay retailers for facilities or services the manufacturer makes equivalent payments available on proportionally equal terms to all other competing retailers. 15 U.S.C. § 13(d) (2000). Although there are limitations in its applicability,

extract special treatment from a manufacturer Category Captain may present Robinson-Patman complications.

While it may appear that the legal inability to charge different customers different prices may hinder firms, Congress accounted for this as well. Section 2(b) provides an affirmative defense to violations of Section 2(a) and Section 2(e) for firms that price discriminate for the sole purpose of competing with a second price-cutting firm. This “meeting competition defense” precludes liability when the “lower price or the furnishing of services or facilities [is] made in good faith to meet an equally low price of a competitor, or the services or facilities furnished by a competitor.”<sup>209</sup> Furthermore, firms are permitted to argue that price differentials were cost-justified when faced with a Section 2(a) challenge, but are not when charged with a violation of Section 2(e).<sup>210</sup>

Exactly what constitutes a service or facility is relatively intuitive, and the Code of Federal Regulations lists category management types of services as included in the Act’s restrictions. These include: “Co-operative advertising; Handbills; Demonstrators and demonstrations; Catalogues; Cabinets; Displays; Prizes or merchandise for conducting promotional contests; Special packaging, or package sizes,”<sup>211</sup> related to the reselling of a good.<sup>212</sup> Therefore, in practice it appears that to avoid a prima facie violation of Section 2(e) of the Robinson-Patman Act a Category Captain must provide its services to all competing retailers on proportionally equal terms.<sup>213</sup>

for the purposes of this discussion Section 2(f) is treated as though it expressly prohibits a buyer from knowingly receiving or inducing discriminatory services under Section 2(e).

209. 15 U.S.C. § 13(b) (2000). The Supreme Court has noted that:

In most situations, a showing of facts giving rise to a *reasonable belief* that equally low prices were available to the favored purchaser from a competitor will be sufficient to establish that the seller’s lower price was offered in good faith to meet that price. In others, however, despite the availability from other sellers of a low price, it may be apparent that the defendant’s low offer was not a good-faith response.

Falls City Indus., Inc. v. Vanco Beverage, Inc., 460 U.S. 428, 439 (1983) (emphasis added); *see also* Walker v. Hallmark Cards, Inc., 992 F. Supp. 1335, 1340–41 (M.D. Fla. 1997) (holding, *inter alia*, that a supplier may offer one customer a larger value of promotional materials than a second if the supplier relies on a trusted source’s personal knowledge that its competitor is providing the first customer with a similar deal). The “meeting competition defense,” as it is called, simply means that the firm acted the way it did because its competitor did so first and in order to remain competitive, the first firm needed to respond in kind.

210. WILLIAM C. HOLMES, ANTITRUST LAW HANDBOOK 546–47 (2002 ed. 2001).

211. 16 C.F.R. § 240.7 (2004).

212. *Id.* at § 240.2(a)(5) (2004).

213. A Section 2(e) violation also requires that the services provided be related to the resale of goods. Category Management services, by definition, meet this requirement. As discussed, however, Section 2(e) violations do permit for a meeting competition defense. Nevertheless, it is

While the Federal Trade Commission, through the Fred Meyer Guides,<sup>214</sup> provides ample explanation for what constitutes proportionally equal terms,<sup>215</sup> case law provides little instruction on how the Guides should be applied to Category Management type services.<sup>216</sup> The Fred Meyer Guides were developed as a reaction to discrimina-

not at all clear that Category Captains could use the defense on an ongoing basis as a guise to continuously price discriminate.

214. 16 C.F.R. § 240.1 (2004) (instructing that “The purpose of [the Fred-Meyer] Guides is to provide assistance to businesses seeking to comply with sections 2 (d) and (e) of the Robinson-Patman Act”).

215. *Id.* at § 240.9. This Section provides that:

(a) Promotional services and allowances should be made available to all competing customers on proportionally equal terms. No single way to do this is prescribed by law. Any method that treats competing customers on proportionally equal terms may be used. Generally, this can be done most easily by basing the payments made or the services furnished on the dollar volume or on the quantity of the product purchased during a specified period. However, other methods that result in proportionally equal allowances and services being offered to all competing customers are acceptable.

(b) When a seller offers more than one type of service, or payments for more than one type of service, all the services or payments should be offered on proportionally equal terms. The seller may do this by offering all the payments or services at the same rate per unit or amount purchased. Thus, a seller might offer promotional allowances of up to 12 cents a case purchased for expenditures on either newspaper advertising or handbills.

*Id.*

216. While there appears no case law directly on point, case law in similar situations suggests that a court faced with a challenge would require the Captain manufacturer to demonstrate that it offered services on a proportionally equal basis. *See, e.g., Alterman Foods, Inc. v. FTC*, 497 F.2d 993, 995 (5th Cir. 1974) (holding that “a wholesaler and retailer of groceries and household products violates the Federal Trade Commission Act by inducing its suppliers, at their own expense, to participate in a food show for its buyers and customers, knowing that the suppliers did not so cooperate with its competitors”). The FTC has since signaled its disagreement with the *Alterman* court’s reasoning, but primarily on the grounds that the challenged trade show services did meet the Act’s requirement that the discrimination relate directly to the resale of goods. *In re. Gibson*, No. 9016, 1980 WL 338971, at \*1, \*181 (F.T.C. April 30, 1980).

Section 2(d) does not refer to benefits to ‘favored buyers’ in connection with the original sale to the buyer, such as discounts, nor does it refer to a seller who charges different prices to different buyers according to the qualification or functional level of the buyer; rather it refers to payments in connection with the resale by the buyer of the goods, for advertising, promotion or other similar purposes.

*Id.*; *see also In re. Max Factor & Co.*, No C-3201, 1986 WL 722142 (F.T.C. Oct. 15, 1986) (challenging Max Factor’s “paying or contracting to pay to or for the benefit of any customer anything of value as compensation or in consideration for advertising or promotional services or facilities furnished by or through such customer in connection with the advertising,” the FTC held that under § 2(d) a manufacturer must provide alternatives such as “handbills and circulars [], or other in-store promotional activities”). Moreover, paying retailers for advertising has been recognized by courts to be a means of achieving indirect price discrimination. *See Hygrade Milk & Cream Co., Inc. v. Tropicana Products, Inc.*, No. 88 Civ. 2861, 1996 WL257581, at \*1, \*3 (S.D.N.Y. May 16, 1996); *American Booksellers Ass’n, Inc. v. Barnes & Noble, Inc.*, 135 F. Supp. 2d 1031, 1068 (N.D. Cal. 2001) (noting that “[a] promotional allowance provided by a seller to a buyer that bears little relationship to the buyer’s actual advertising costs provides a cash windfall to the favored buyer and, thus, can only be viewed as a reduction in the buyer’s cost of goods”). Given courts’ focus on the value conferred to retailers as a means of indirect price discrimination it is not a stretch to conceive of a challenge to disproportional value conferred by means of Category Management services.

tory price discounts received by the Fred Meyer grocery chain.<sup>217</sup> They provide recommendations on how a grocer or manufacturer can effectively comply with the requirements of the Robinson-Patman Act. While they do not have the force of law, the Guides instruct that,

[a] seller who makes employees available or arranges with a third party to furnish personnel for purposes of performing work for a customer should make the same offer available on proportionally equal terms to all other competing customers or offer useable and suitable services or allowances on proportionally equal terms to competing customers for whom such services are not useable and suitable.<sup>218</sup>

Despite the lack of case law so mandating, the Guides make it relatively clear that a manufacturer needs to be certain that if it chooses to serve as a Category Captain for a large retailer it also makes available at least some category management services to even its smallest customers.

Nevertheless, while case law does not directly instruct a manufacturer how to create a program that offers Category Management services on proportionally equal terms, it *does* instruct that the services must be similar in kind and magnitude.<sup>219</sup> When camera manufacturer Minolta instituted a program by which it provided its preferred retailers with free advertising, free cameras and camera equipment, and free promotions, non-preferred camera retailer Alan's of Atlanta sued.<sup>220</sup> Minolta desired to focus its marketing and merchandising efforts on its largest retailers, seeking to increase its efficiency.<sup>221</sup> The value of benefits that Minolta provided to preferred customers amounted to nearly \$0.03 for every dollar worth of Minolta goods the customer purchased. Minolta also offered the plaintiff financial benefits in the form of favorable credit terms, but only in the range of \$0.0087 for every dollar in Minolta goods purchased.<sup>222</sup>

The court asserted that the programs' terms were not proportionally equal for three reasons. First, the credit terms provided to Alan's of Atlanta were different in kind from the free goods and

217. See *FTC v. Fred Meyer, Inc.*, 390 U.S. 341 (1968).

218. 16 C.F.R. § 240.9(b) (Example 5) (2004).

219. See *Alan's of Atlanta, Inc. v. Minolta Corp.*, 903 F.2d 1414 (11th Cir. 1990).

220. *Id.* at 1416.

221. *Id.*

222. *Id.* at 1422-23.

promotional funds provided to Minolta's preferred customers.<sup>223</sup> Second, Minolta's program prohibited the plaintiff from participating in the favored programs, but did not exclude favored retailers from receiving the same favorable credit terms as Alan's of Atlanta.<sup>224</sup> Finally, the programs were not proportionally equal because they provided vastly different value as a ratio to dollars spent on Minolta goods.<sup>225</sup>

*Alan's of Atlanta* provides guidance to Category Captains seeking to comply with the mandates of the Robinson-Patman Act. It first teaches that the Category Management services or programs that it provides to smaller retailers must be similar in kind to those offered to larger retailers. For instance, it would likely be problematic to offer Category Management planning and implementation services to one retailer, but only favorable credit or delivery terms to a second. Second, it instructs that it is not sufficient to merely provide smaller retailers with what may seem like a fair alternative program. Rather, it is necessary to take the extra step to calculate the value of services it provides as Category Captain and the value of lesser services, and then determine a way to offer them on an equal basis. This may present problems when a single manufacturer provides identical Captainty services to two large retailers that purchase a measurably different quantity or dollar value worth of goods.

With the recent increase in market concentration amongst consumer product retailers, market conditions resemble those feared by Representative Patman when he devised the Robinson-Patman Act. Patman was concerned with large retailers leveraging their scale to coerce from manufacturers price cuts that were not justified by increased order size. Certainly, in light of Captainty fees charged by some retailers, one interpretation of the Category Captain relationship is that it may be a veiled attempt to exude indirect price discrimination from manufacturers. Nevertheless, market power in the manufacturing sector may provide still another explanation—a desire to gain favorable treatment at the retailer.

Many firms, however, are interested simply in improving the efficiency of a retailer's product categories. Manufacturers must there-

223. *Id.* at 1424. The court determined that there was an inherent difference between credit terms, used to purchase a good, and thus not within the purview of Sections 2(d) and 2(e), and advertising and promotional programs, which directly relate to the resale of goods. *Id.*

224. *Id.*

225. *Id.* The court in *Alan's of Atlanta* did not assert that retailers must always provide benefits in exact proportions, but rather that this was a benchmark.

fore devise Category Management programs that ensure proportionally equal service to all customers. Part V of this Note provides several recommendations.

## V. RECOMMENDATIONS

Category management is, at least for now, a practice deeply entrenched in the supermarket industry, and as a business practice presents a valuable means by which a retailer may navigate through an endless maze of seemingly identical products. Nevertheless, the gray-ing of the once bright line between vertical and horizontal relationships presents a unique challenge for antitrust practitioners. There is, without a doubt, an opportunity for vertically related firms to collaborate for mutual benefit but each needs to monitor their activity to ensure that each complies with both the Sherman Act and the Robinson-Patman Act. Parties should be careful to structure their relationships in a way that achieves the benefits of the Category Captain relationship, but minimizes the anticompetitive risk.

The directives of the Sherman Act are quite benign, and even the least sophisticated manufacturers and retailers should have no trouble adapting their business practices to comport with them. First and foremost, manufacturers and retailers should resist the temptation to collaborate in setting retail prices.<sup>226</sup> This practice is ripe for antitrust litigation, much of which yields a per se violation of the Sherman Act.<sup>227</sup> Nevertheless, some minor business process reengineering can serve to minimize risks. Firms can still benefit from the collaborative nature of the Category Captain relationship without ever discussing price. For instance, a manufacturer could train any given retailer to perform the necessary calculations on its own and, where applicable, provide promotional funds to pay for data costs.<sup>228</sup> The manufacturer could also provide the retailer with third-party software to perform the necessary calculations.<sup>229</sup> Under this scenario, the Category Captain would still provide the manufacturer with beneficial Category

226. *Supra* Part IV.

227. *Id.*

228. This, of course, is a perfectly legal alternative. *Maple Flooring Mfrs. Ass'n v. United States*, 268 U.S. 563 (1925).

229. See, e.g., AC Nielsen, *What is Priceman?*, <http://www.acnielsen.com/products/tools/priceman/> (discussing AC Nielsen *Priceman* software that enables firms to make data-based pricing decisions) (last visited March 14, 2004).

Management services but would not proffer direct price recommendations.

Secondly, retailers should take affirmative steps to monitor manufacturers to ensure ethical behavior, as the retailer itself may become liable for a supplier's behavior under Section 1 of the Sherman Act. Although there is a fine line between vigorous competition and antitrust violation, it seems relatively apparent when the line has been crossed. Retailers possess numerous means by which to achieve this. At minimum, the retailer could seek input from competing manufacturers to ensure accurate category recommendations.<sup>230</sup>

Retailers could also eliminate all Category Captain relationships and instead demand better prices, using the savings to staff stronger category management teams to make such decisions internally.<sup>231</sup> This scenario would make it simple to remove all possibility of collusive behavior, as the retailer would assume responsibility for Category Management decisions.<sup>232</sup> This is less appealing, however, to the manufacturer, as it provides no guarantee that a retailer will invest the savings into Category Management. To rectify this dilemma, manufacturers could instead provide promotional funds conditioned on Category Management activities. This would permit the manufacturer a degree of certainty that the funds are paid for the Category Management work and not for favorable shelf space, as well as the flexibility to revoke funding if they are not.

Furthermore, the retailer could instead demand that the Category Captain manufacturer itself fund an independent external consultant. In this scenario, it would be useful for the manufacturer to provide funds to the retailer, which would then pay the consultant.<sup>233</sup>

230. This is the practice of the Ukrop supermarket chain. *FTC Slotting Day 2*, *supra* note 1, at 354.

231. While it may be true that under present business structures, manufacturers may be a more natural fit to specialize in their category than a retailer, *see generally* Steiner, *supra* note 11, at 80, it very well may be that this is because the retailers have not been asked to perform the work on their own. It is likely that manufacturers are better because they have more employees dedicated to each relevant category. Certainly, retailers are capable of managing categories on their own. For instances, the Stop & Shop grocery chain does not make use of Category Captains or lead manufacturers, but relies on its own personnel to reach decisions. *See FTC Slotting Day 2*, *supra* note 1, at 326-27.

232. This would also make it much easier for a manufacturer to comply with Robinson-Patman requirements.

233. Third party Category Management companies are quite prevalent. A brief Internet search reveals numerous options. On the strategy and planning side, there is AC Nielsen, *see* <http://acnielsen.com/services/category/camansol.htm> (discussing AC Nielsen's various consulting services), and Winston & Weber Associates, Inc., *see* <http://www.winstonweber.com/>. On the in-store implementation side there is the Merchandising Corporation of America, *see*

This would eliminate any aversion on behalf of the third party to provide inaccurate work in a desire to please the party footing the bill.<sup>234</sup> It seems that this scenario does the most to eliminate risk of each party abusing the relationship. The independent consultant would work for the retailer, as the Category Captain claims to do, and the manufacturer would still absorb the cost. In this scenario, there is no opportunity for manufacturer and retailer to collude on price. There is also no incentive for the third-party Category Manager to deceive the retailer.

While it is relatively clear how to alter the Category Captain relationship to comply with the Sherman Act, comporting with the Robinson-Patman Act is somewhat less clear-cut, primarily because there is little case law by which to guide business decisions. Nevertheless, the same modifications to Category Captain that would serve to ensure compliance with the Sherman Act programs will aid in compliance with the Robinson-Patman Act. The safest bet, of course, would be for retailers to staff stronger category management teams to make such decisions internally and demand better prices from manufacturers.

As with compliance with the Sherman Act, however, the most effective paradigm is for a manufacturer to fund a third party Category Manager.<sup>235</sup> Here, it would be simple to measure the exact value of the service provided to each retailer. Therefore, determining whether the services are provided on proportionally equal terms would be much easier than today. Furthermore, Congressional or Administrative action may be necessary to clarify the boundaries. Most helpful would be an updated version of the Fred-Meyer guidelines focusing on Category Management services.

In the end, a balance needs to be reached whereby the most efficient actor performs retail-level Category Management decisions in a way that best serves consumers and protects competition. The safest way from an antitrust perspective is to shift the work back to the retailer or to a third party.

<http://mcaretail.com/services/index.asp>, R&R Marketing Services, Inc., see [http://www.rrmarketingservices.com/wst\\_page5.html](http://www.rrmarketingservices.com/wst_page5.html), and National In-Store, see <http://www.nis-online.com/merchandising.asp>.

234. Tosh, *supra* note 23, at 90 (relating the view of one expert that “a third-party company is ‘directed by the retailer’ and does not have a vested interest in one particular branded product”).

235. See *supra* note 232.