No. 02-603

IN THE

Supreme Court of the United States

UNITED STATES TOBACCO COMPANY, UNITED STATES TOBACCO SALES AND MARKETING COMPANY, INC., UNITED STATES TOBACCO MANUFACTURING COMPANY, INC., UST, INC.,

Petitioners,

v.

CONWOOD COMPANY, L.P., CONWOOD SALES COMPANY, L.P.,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

BRIEF OF THE AMERICAN WHOLESALE MARKETERS ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF PETITIONERS

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November 20, 2002

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INTEREST OF THE AMICUS CURIAE[1]

The American Wholesale Marketers Association ("AWMA") is a non-profit, trade association located in Washington, D.C., whose primary members are wholesaler-distributors serving the convenience store

[1] Pursuant to Sup. Ct. R. 37.6, the American Wholesale Marketers Association states that no counsel for a party has authored this brief in whole or in part, and that no person or entity, other than the AWMA, has made a monetary contribution to the preparation or submission of this brief. Pursuant to Sup. Ct. R. 37.3(a) AWMA states that the parties of this proceeding have consented to the filing of this brief.

industry in the United States. AWMA wholesaler-distributor members represent more than 85 billion dollars in United States convenience product sales. The AWMA has over 400 wholesaler members, and there are another 600 non-member wholesaler businesses also servicing the convenience store industry. Associate members include manufacturers, brokers, and retailers. The variety of consumable products sold to convenience store retailers by AWMA members includes candy, tobacco, snacks, beverages, general merchandise, and food service.

While AWMA wholesaler members primarily sell to the convenience store chain, they also service other consumer outlets, such as grocery stores, drug stores, tobacco shops, and gasoline merchants. AWMA wholesalers often provide the primary, if not the only, means for manufacturers, especially those with smaller market share and fewer resources, to move their products to the ultimate consumer. Typically, wholesalers provide an excellent means by which many manufacturers can competitively place their products before consumers.

This brief is filed only in support of the petitioners' United States Tobacco Company, et al. ("USTC") request that the Supreme Court issue a writ of certiorari. Both the respondent Conwood Company, L.P., et al. ("Conwood)" and petitioner USTC are Associate manufacturer members

of the AWMA.[2] This AWMA *amicus* brief only relates to the first question[3] presented by USTC, *i.e.*:

> Whether liability under section 2 of the Sherman Act, 15 U.S.C. § 2, may be based on a manufacturer's misleading "suggestions" and "recommendations" to retailers where there is no foreclosure of the competitive process or of a substantial portion of the market.

STATEMENT OF RELEVANT MATTERS NOT ALREADY BEFORE THIS COURT

The AWMA's interest is that many of the trade practices discussed in detail in the *Conwood* decision, which upheld a determination of the defendant's violation of Section 2 of the Sherman Act, are used by and practiced regularly by wholesalers. Thus, the AWMA, seeking certainty in the marketplace for its members, is filing this *amicus* brief to attempt to clarify what trade practices shall be acceptable, reasonable, and appropriate in the convenience store chain of trade, whether implemented by

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[2]The AWMA takes no position regarding the ultimate determination of liability of the petitioner USTC to the respondent Conwood. The purpose of this brief is to set forth AWMA's concerns on behalf of wholesalers that previously acceptable trade practices are now in question and may be reviewed differently by the courts as a result of the exhaustive treatment accorded the convenience chain of commerce in *Conwood Co. v. United States Tobacco Co.*, 290 F.3d 768 (6th Cir. 2002).

[3]Thus, the AWMA makes no comment on any issue relating to damages.

direct seller manufacturers or wholesalers. The AWMA is concerned that the *Conwood* decision could be applied to any person which is dominant in a relevant geographic or product market, with the result that AWMA wholesalers could be substantially affected.

Wholesaler distributors generally continue to play an important and relevant role in marketing channels and supply chains. A recent publication by the National Association of Wholesalers ("NAW") notes that, "[i]n 2000, sales of all wholesaler-distributors reached $2.8 trillion." Adam J. Fein, The Forces of Change Remain, *in Facing the Forces of Change: Outlook 2003* ix (Adam J. Fein, ed., 2002). Growing at a rate of 5.6% since 1991, wholesalers in all categories account for one in every 20 jobs in the United States and 7% of the entire national income. The NAW has determined that 75% of all product sales occur through distributors in a number of trade categories, including food service products. *Id.* at xi.

Usually, wholesalers are independent of manufacturers. The wholesaler relationship to the manufacturer can be likened to that of an agent in some instances and as a direct competitor in others (especially when the manufacturer is a direct seller). The wholesaler promotes a manufacturer's products, pushes its advertising, and passes through financial allowances, when appropriate. While one would never claim that relationships between manufacturers and wholesalers are always agreeable, friendly, and "professional," usually the wholesaler is the good "foot soldier" for the manufacturer. The financial success of the wholesaler is dependent upon

its ability to promote and sell a manufacturer's product. The NAW has stated:

> Manufacturers and distributors continue to rely on each other's actions and resources. Simultaneously, each side struggles to maintain autonomy and control over its own operations. . . . This mutual dependency creates conflicts about direction, strategy and commitments. Business relationships between manufacturers and distributors are not altruistic, nor should they be. Both parties need to perceive a benefit from the relationship.

Id. at xiii.

Trade practices of manufacturers quickly become those of wholesalers who add value by becoming category (product line) managers, creating promotions, assisting in the implementation of manufacturer promotions, providing sales information to retailers and manufacturers, assisting with retailer marketing, and, especially with regard to smaller and newer manufacturing enterprises, providing what may be the only avenue of market penetration. These competitive services, discussed in detail by the *Conwood* court, are the result of many years of business experience and development. The AWMA concern is that these previously accepted practices may no longer be appropriate and that wholesalers in a given economic market may be subjected to antitrust and, possibly, other actions for previously acceptable activities.

ARGUMENT

The *Conwood* decision deals with numerous day-to-day business practices used by wholesalers serving the convenience store industry. In one way or the other, category management is used by all convenience wholesale distributors. Various components which typically constitute category management were discussed in detail by the *Conwood* court. The misuse of category management, which is intended to assist a retailer in its operations, was specifically found to support a violation of the antitrust laws. It is important, particularly in the relevant chain of trade of AWMA members, that the wholesaler distributor clearly understands what the acceptable limits of category management are in today's markets. It is principally for this reason that the AWMA requests the Supreme Court issue the subject writ of certiorari.

Conwood can be read as condemning overly aggressive sales managers acting as category captains and/or managers, excessive "puffery", and extensive allowances and promotional payments under Section 2 of the Sherman Act. If this understanding is correct, then AWMA wholesalers need to know and understand what is, and is not, permissible under the antitrust laws. While an absolute outline of permissible activities is not reasonably expected, any guidance that the Supreme Court can provide this rapidly changing and growing marketplace would afford a certainty around which such businesses can base their competitive practices.

AWMA submits that the holding in *Stearns Airport Equip. Co. v. FMC Corp.*, 170 F.3d 518 (5th Cir. 1999) conflicts with the *Conwood* holding. The Fifth Circuit in *Stearns* stated:

> All of these arguments made by FMC to its potential customers may have been wrong, misleading, or debatable. But they are all arguments on the merits, indicative of competition on the merits. To the extent they were successful, they were successful because the consumer was convinced by either FMC's product or FMC's salesmanship.

Id. at 524.

> Ultimately, Stearns does not and cannot claim that it has been excluded from competing on the merits. Every sales pitch and every suggestion that FMC made was evaluated by independent municipal actors who were concerned solely with the merits of the product they were charged with evaluating. Stearns was free to engage in identical tactics and tout the virtues of its product.

Id. at 527.

The Sixth Circuit in *Conwood* accepted the legal position that the cumulative effect of numerous tortious activities may rise to the level of a violation of the antitrust

laws, and a monopolist's collective tortious activities in a relevant market may properly be held to be a violation of Section 2 of the Sherman Act. It stated that:

> USTC contends that none of the practices Conwood complains of amount to antitrust violations, but are no more than isolated sporadic torts. We disagree. Conwood presented evidence that beginning in 1990, USTC began a systematic effort to exclude competition from the moist snuff market. Conwood presented sufficient evidence that USTC sought to achieve its goals by excluding competition and competitors' products by numerous avenues.

290 F.3d at 783.

In one case, bad acts by a competitor were found not sufficient pursuant to the antitrust laws, and in the other case, bad acts by a competitor were found sufficient to allow them to go to a jury, which found such actions illegal under Section 2 of the Sherman Act. While *Stearns* dealt with the ability of a small airport equipment manufacturer to compete against a substantial monopolist, the *Conwood* case deals with a trade area in which AWMA wholesalers are significantly involved. It appears that the *Stearns* and *Conwood* standards conflict to such an extent that there has been created an uncertainty in the convenience distribution channel. Thus, the AWMA and its wholesaler members have a significant interest in the determination of acceptable business activities which may be used in the convenience store chain.

The *Conwood* court states that "the first step in any action brought under Section 2 of the Sherman Act is for the plaintiff to define relevant product and geographic markets in which it competes with the alleged monopolizer." 290 F.3d at 782, citing *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 268-69 (2d Cir. 1979). The court also notes that "[a] geographic market is defined as an area of effective competition." 290 F.3d at 782, citing *Re/MAX Int'l., Inc. v. Realty 1, Inc.*, 173 F.3d 995, 1016 (6th Cir. 1999). While the *Conwood* decision applies to a nationwide manufacturer controlling 75 percent of the relevant market, its analysis would apply to any firm holding a dominant position in "an area of effective competition."

The *Conwood* court listed a number of specific USTC business practices that were impermissible, probably tortious, and which, when combined, were sufficient to uphold the Section 2 violation. Such practices included: 1.) removing Conwood sales racks and placing Conwood product lines in USTC racks to "bury" Conwood's products and reduce Conwood facings, 2.) using various "ruses," such as obtaining permission to reorganize and neaten any moist snuff section so as to destroy competitors' racks, 3.) misusing its category manager status by providing false and misleading information to retailers, and 4.) entering into exclusive agreements with retailers in an effort to exclude Conwood products.

The Court then criticized at length as impermissible exclusionary conduct under Section 2 of the Sherman Act various sales, marketing, and business practices employed

by USTC, *id.* at 774-780, which AWMA submits are utilized daily by its wholesaler members. The interest of the AWMA and its members is that all the various marketing practices discussed are used to supply product to the convenience store chain. While the wanton destruction of a competitor's property and tortious activity interfering with a competitor's ability to do business have been and should continue to be illegal under any number of theories, including common law tort and state fair trade laws, the following, discussed at length by the Sixth Circuit, have been acceptable trade practices[4].

1. The use of racks to display, hold, and market product is common in any commercial enterprise. While "facings" here dealt with slots in sales racks, the facings for other products presented to the consumer are carefully developed for many kinds of products. Although racks are discussed in *Conwood,* metal or wood stands, "lazy susan" displays, and coffee bean dispensers are other examples which are touted by manufacturers through wholesalers to retailers in any number of formats with any number of arrangements, deals, and promotions. The use of one distributor's display method over another's often involves contentious competition among competitors. It is not uncommon for distributors to pressure retailers

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[4] At the end of the discussion of USTC trade practices, the *Conwood* court discussed unauthorized rack removals by USTC, *id.* at 778-779. This practice is not common and has never been considered a legitimate business practice. It is not discussed in this brief as anything other than recognition of its being an unethical, if not tortious, activity.

to use that distributor's (or manufacturer's) display mechanism exclusively. In any event, the final decision regarding display methods should be left to the affected retailer.

2. Point-of-Sale ("POS") advertising is used extensively by various category managers to promote their products. As *Conwood* recognized, POS advertising is acutely critical to tobacco advertising, since such advertising is restricted outside a retail outlet. *Id.* at 774. POS advertising is also important for soft drinks and snacks, because it may identify the product's location in the store and indicate promotions which may exist. Wholesalers are often encouraged by manufacturers, which provide significant financial incentives to promote their products, to place POS advertising materials at retailers' establishments.

3. Category management[5] entails all elements of placing product in a retail outlet to most effectively induce favorable consumer response--a purchase. Wholesalers provide this service to many retail stores, and AWMA members particularly provide this to the convenience store chain. Depending on many factors, such as size, location, product mix, customer needs, and profitability, wholesalers will often provide this service to their convenience store customers. With wholesalers, category

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[5]The use of category captains was discussed by the *Conwood* court. The AWMA is unaware of this being a common tool used by wholesalers.

management can relate to a single product or to the bundling of different products and product lines. In any event, the intent is to maximize sales to the ultimate consumer. As the *Conwood* court discussed, many tools are used, such as allocating shelf space based on sales volume and the use of plan-o-grams, which are also used by wholesalers.

4. The *Conwood* court specifically discussed the role of category managers in the moist snuff trade. *Id.* at 785-787. Among other things, USTC, as the dominant competitor in the moist snuff category, would suggest that fewer moist snuff products (SKUs) be carried, usually pressuring that its competitors' products be limited or discontinued. USTC would attempt to limit price value brands[6]. The AWMA notes that, while the use of category managers is common with manufacturers, it is also a widely accepted practice within the convenience store chain wholesale business. Because wholesalers are involved with many products, they may "bundle" products, provide information on various products, pass through or create their own incentive programs, and assist their customers with such diverse marketing techniques as rack and product placement, sales data collection and distribution, and product analysis. It is not unusual for a wholesaler, often at the urging of its retailer

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[6] Price value brands typically are generic brands which sell for substantially less than a premium brand. Most often, it is a store brand which is placed near a brand name item, the store brand always being cheaper.

customer, to limit the number of product SKUs it carries in order to limit costs and inventory.

5. *Conwood* discussed the role of USTC in its attempts to remove price value products. AWMA wholesalers have battled each other for years on which product should be placed where in any retail outlet based on the product's value. In the cigarette business, there is a constant disagreement, i.e., competition, between those distributors selling what are known as third and fourth tier (cheaper) cigarettes and those promoting premium brand cigarettes. Likewise, there is a constant pressure being placed on retailers with regard to the store placement and sale of cheaper, bulk (generic) candy products versus name brand, more expensive confectioner products. The competition between value priced and premium quality products has been ongoing for many years, especially as the prices for premium products have increased.

6. USTC started its Consumer Alliance Program ("CAP") in 1998. *See Conwood* at 778. USTC gave retailers a promotional allowance for providing USTC with certain sales data and for participating in various promotional programs. This business practice is commonplace in the wholesale chain. An AWMA wholesaler will either participate in a manufacturer's incentive program and pass through part of the allowance to the retailer or implement a program of its own for its convenience store customers. There is little question that this technique is used to enhance the

> sale of a particular product or to induce a retailer to trade with a particular wholesaler or manufacturer.

The *Conwood* decision, its effect, and its rationale are just now becoming known in the antitrust legal field and in the wholesale-distributor industry. While various questions are now being raised, it would appear that the effects on three interrelated business practices--shelf space competition, category management, and POS advertising--are being discussed. For instance, in an article to be published in the ABA Antitrust Magazine, it was stated that:

> The importance of product display (and accompanying POS advertising) to competition in the moist snuff market was central to the Sixth Circuit's conclusion that USTC had violated Section 2 by persuading retailers to display its products more prominently than those of its competitors. That consideration, however, could as easily support a contrary argument: If product placement and POS advertising are the areas where competition takes place, they are the areas where competitors should legitimately focus their efforts.

Dennis Cross, *Monopolization or Competition? Reporting Snuff Wars,* ABA Section on Antitrust Law, 17 Antitrust Magazine (forthcoming 2002) (manuscript on file with author, at 6).

The issue relates to the extent to which companies and their sales force may focus their product promotion. In any retail operation in the United States, the placement of product and the relevant POS advertising become an issue of overriding concern and interest to the manufacturer, wholesaler and retailer. The more prominently a product is displayed and advertised to the consumer, the more likely it is that the consumer will purchase such item. In the AWMA wholesale chain, primarily directed at the convenience store market, this is the simplest explanation for what dictates wholesaler actions. From a rural convenience store in the Midwest to corner stores in New York City to even small kiosks on Capitol Hill, virtually every consumer purchases something--a candy bar, a quart of oil, a package of razor blades, a pack of cigarettes, a donut, or a cup of coffee--which probably has been distributed by a wholesaler. Although the ultimate decision is up to the retailer, the placement of each product, the amount of shelf space allocated, the promotions offered, and product merchandising are usually supported, developed or presented by a wholesaler for itself or, directly or indirectly, on behalf of a manufacturer.

Many of the sales practices employed by AWMA members were reviewed by the *Conwood* court. While there is no place in the marketplace for the outright destruction of competitors' property and for any knowing and material fabrication of sales data, many of the practices discussed in *Conwood* are customary. Most wholesalers would find it impossible to determine when information "puffery" on such diverse matters as quantity,

quality, consumer preference, sales data, and research, becomes illegal fabrication.

CONCLUSION

It appears that the *Conwood* decision is the first to detail sales practices of AWMA wholesalers which sell equivalent product lines to the same retailers who may also be served by manufacturers. It may be appropriate now to redefine and delineate future legitimate and acceptable business practices in this line of trade. In order to maintain a competitive process allowing wholesalers to compete with various manufacturer direct sellers, as much specificity regarding acceptable business practices and the consequences for such improper and illegal business methods must be established. If previous business practices, illegal under various local and state laws, common tort law, and fair trade statutes, can *in toto* rise to the level of an antitrust violation, the Supreme Court can now establish what the limits of acceptable competition are.

For all of these reasons, the Supreme Court should issue this writ of certiorari.

Respectfully submitted,

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