Exclusivity: The Right and

It's not anticompetitive, *per se*

By Gordon Schnell

With the recent indictment by New York State Attorney General Eliot Spitzer of James Zimmerman, former head of Federated Department Stores, the retail industry has received a stark wake-up call on the risks associated with exclusive dealing. Zimmerman's indictment follows on the heals of Spitzer's successful challenge to an exclusive-dealing arrangement among Federated (owner of Macy's and Bloomingdale's), May Co. (owner of Lord & Taylor and Filene's), Lenox and Waterford Wedgwood for the sale of Lenox china and Waterford crystal. The parties paid a substantial fine (roughly $3 million) and entered into an antitrust consent decree to settle Spitzer's charges.

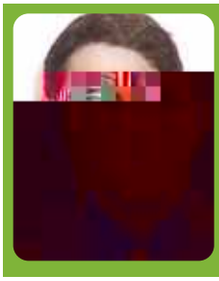
While entering into exclusives with key suppliers has been a hallmark of retail trade for generations, merchants may now be wary of relying on the prevalence of this industry practice in negotiating exclusives going forward. And for good reason. Spitzer has made a name for himself by exposing industry practices that, while pervasive, are questionable in their legality and their ultimate effect on consumers.

The potential pitfalls associated with exclusive-dealing arrangements principally arise out of Section 1 of the Sherman Act, which prohibits agreements or conspiracies that unreasonably restrain trade. An exclusive deal between a retailer and supplier does not in and of itself violate this proscription. On the contrary, for more than 80 years the Supreme Court has recognized as paramount a company's right to choose with whom it wants to deal.

Furthermore, while exclusivity will obviously diminish competition on an intra-brand basis (competing sellers of the same brand), it actually can foster competition on an inter-brand basis (competing brands). In particular, exclusivity allows the chosen seller to expend considerable resources on selling the product without fear that competing sellers will get a free ride on these efforts. Suppliers can greatly benefit from having a limited number of distributors committed to selling their brand. That is why exclusivity deals typically involve promotional obligations on the part of the seller. Exclusivity also can provide the supplier with greater control over how and where the brand is sold. All of this can lead to stronger competition among rival brands.

The area where exclusivity can lead to trouble is when it becomes the centerpiece of a directed effort by a group of retailers or suppliers to suppress competition from one or more of their competitors. That is exactly what happened in the Lenox/Waterford deal. According to Spitzer, Federated and May Co. secured the exclusive deal for the purpose of preventing Bed Bath & Beyond from selling the Lenox/Waterford products. Such a scheme epitomizes the classic group boycott—two or more sellers getting together to persuade or coerce a key supplier to stop dealing with the sellers' competitor to suppress competition from that seller.

But not all group boycotts violate the antitrust laws. And in the context of retail trade, the line that separates those that do from those that don't can be particularly murky. The trick for retailers is to make sure their arrangements fall outside of the purview of per se antitrust review. As long as they do, it's a pretty safe bet that their exclusives will escape antitrust attack. For



> "A boycott that involves concerted, rather than independent, action by competitors is bound to lead to trouble."
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