Vertical Restraints Part 1 (Exclusive Dealing)

Antitrust
Eric E. Johnson
ericejohnson.com

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Requirements contracts / exclusive supply contracts (1/2)

- The phrases "requirements contracts" and "exclusive supply contracts" are terms for an agreement whereby a supplier and buyer agree that over a certain term (e.g., one year) a buyer will only buy a certain something from the supplier, and the supplier will meet the buyer's requirement to be supplied.
  - Typically, this might involve a fixed price.
- Formerly, these arrangements, if large in scale, got strong pro-plaintiff treatment via an interpretation of Clayton Act § 3, that such arrangements are illegal if they "foreclose[] ... a substantial share of the line of commerce affected." *Standard Stations Case*, Standard Oil and Standard Stations v. U.S., 337 U.S. 293 (1949).

Requirements contracts / exclusive supply contracts (2/2)

- Later, SCOTUS moved to a regular rule-of-reason analysis in *Tampa Electric v. Nashville Coal* (1961):

  > "To determine substantiality in a given case, it is necessary to weigh the probable effect of the contract on the relevant area of effective competition, taking into account the relative strength of the parties, the proportionate volume of commerce involved in relation to the total volume of commerce in the relevant market area, and the probable immediate and future effects which pre-emption of that share of the market might have on effective competition therein."

- Lower courts have gone further, holding that "[e]xclusive-dealing contracts terminable in less than a year are presumptively lawful." *Roland Machinery v. Dresser Industries* (7th Cir. 1984) (Posner, J.).

Exclusive dealing – market share foreclosed

After *Tampa Electric v. Nashville Coal* (1961), the emphasis is qualitative. But lower courts have developed a pro-defendant quantitative take: Without a large percentage of a market share being foreclosed, courts will generally refuse to find exclusive dealing to be exclusionary or unreasonable.

- Some courts indicate a minimum of 30-40% of the market must be foreclosed by an exclusive dealing arrangement for antitrust liability.
- foreclosure of 24% unlawful (*Twin City* (9th Cir. 1982))
- foreclosure of 38% lawful (*Omega Envtl.* (9th Cir. 1997))
- foreclosure of 40% lawful (*Gonzalez* (N.D. Ga. 1985))

Courts typically require less foreclosure for § 2 than for § 1. (*Microsoft*, EE[3d]@404):

- foreclosure of roughly 40-50% usually needed for § 1.
- foreclosure of less needed for § 2.

Microsoft's five principles for analyzing whether something is § 2 exclusionary conduct

1. Look at anticompetitive harm to process, not merely harm to individual competitors (i.o.w., harm to competition, not competitors).
2. Plaintiff must demonstrate anticompetitive effect.
3. Defendant may offer procompetitive justifications (e.g., greater efficiency, enhanced consumer appeal).
   - Plaintiff can then rebut this. But if that doesn't work ...
4. Balance the anticompetitive effects against the procompetitive justifications.
5. Focus on the effect of the conduct, not the intent behind it.

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You can use this as a way of thinking about § 2 exclusionary conduct for all § 2 cases, not just exclusive dealing allegations.

Problem

- Sky Lasso provides on-ramp cabin services for passenger airlines, including cleaning, lavatory servicing, restocking of in-flight magazines, etc.
- Currently, neither Sky Lasso nor Oceanic Airlines have any operations at DFW. DFW has many airlines and two on-ramp cabin services firms.
- Oceanic Airlines and Sky Lasso want to expand to DFW.
- They are contemplating a deal where Sky Lasso will be the exclusive supplier to Oceanic Airlines for three years at DFW.

Based on just these facts, is there an antitrust problem with this deal?

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- **No, because there's no indication of market power / strength / amount of market foreclosed, etc. Without that, there really can't be an anticompetitive effects.**

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sky lasso

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- **This commitment could ensure that Sky Lasso will recover its investment on fixed costs of starting operations at DFW - office space, apron space, trucks, start-up hiring/training, etc.**
- **Maybe Oceanic needs to incentivize Sky Lasso to make relation-specific investments, like special equipment for servicing A380s.**

GRENKA GRÜBNER

HOME HANGAR

- Grenka Grübner is a major manufacturer of lawn mowers but currently sells none in the USA.
- Home Hangar has 1,200 big-box home improvement stores across the USA.
- Can they do a deal where Home Hangar will be the the exclusive distributor and retailer of Grenka Grübner mowers in the USA for five years?

Why would the parties want to do this deal?

What's potentially procompetitive about this?

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Why would the parties want to do this deal?

- This encourages HH to invest in TV ads, sales promotions, employee training on selling GG products, etc.
- You could spell all this out in a contract—but it's hard to specify, and even harder to police.
- It's better to just get the incentives right.

What's potentially procompetitive about this?

- This may decrease (or foreclose) intrabrand competition.
- But it increases interbrand competition.

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I tried rewriting the answer to this question to make it less confusing.

What's potentially procompet... e about this?

- It increases interbrand competition, because it brings a new lawn mower brand to the USA. (Although, admittedly, this forecloses future intrabrand competition.)

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