UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF KENTUCKY
AT PADUCAH
CASE NO. 5:98CV-108-R

CONWOOD COMPANY L.P., ET AL. PLAINTIFFS

v. **MEMORANDUM, OPINION AND ORDER**

UNITED STATES TOBACCO SALES
AND MARKETING COMPANY, INC. DEFENDANTS

INTRODUCTION

This antitrust case is before the court on the motion for summary judgment of defendant United States Tobacco ("UST") (Docket#208) and the cross-motion for partial summary judgment of Conwood Company (Docket #207). In this extensively litigated case, Conwood has challenged the moist snuff marketing practices of its rival UST. For the reasons set out below, the court concludes that only through the development at trial of a full factual record can there be an appropriate determination of whether UST's practices concerning exclusive racks and exclusive point-of-sale advertising constitute the illegal maintenance of monopoly power through anticompetitive practices. Likewise, market definition issues cannot be decided without a trial. Accordingly, the court will deny the motions for summary judgment.

FACTUAL BACKGROUND OF THE ANTITRUST LITIGATION

This case involves moist snuff,[1] a form of tobacco used orally by consumers by placing a small amount between the cheek and gum. The product is generally sold in round cans in retail stores, including convenience markets, mass merchandisers such as Wal-mart, and other outlets where snacks, sodas, cigarettes, and other convenience items can be readily bought. The cans are typically kept by the retailer in a gravity-fed rack, so that cans drop down through slots, also

[1]There is an issue at trial concerning product market definition, but for purposes of this analysis, the court will restrict itself to a discussion of moist snuff. See opinion below at 15-16.

called "facings." These racks are often located by the check-out counter. The racks, in addition to storing the cans, also provide a place for point-of-sale advertising, sometimes referred to as "header cards." The number of slots in a rack is significant, as it affects not only the overall size of the rack but the number of products which a customer will see. As is common in consumer product merchandising, the placement of the rack, the arrangement of the point-of-sale advertising, and the display of competiting products within the racks are all areas of competition among moist snuff manufacturers. Each manufacturer wants its product displayed most prominently and strategically, and wants to maximize its point-of-sale advertising.

Point-of-sale advertising is commonplace in convenience merchandising, whether it involves colas, beer, snack foods, or other products. According to Conwood, however, it assumes an unusual importance in the tobacco industry, because of the significant limitations which state and federal law place on media advertising of tobacco products. While consumers can enjoy the antics of the Budweiser lizards or the Energizer bunny, there is no comparable television and radio exposure for tobacco companies. Thus, in the Conwood theory, point-of-sale advertising is especially critical because it represents the principal means of communicating with consumers. In the plaintiff's view, any restrictions on point-of-sale advertising are likely to have a seriously dampening effect on competition.

Conwood asserts that it moved from being a small player in the moist snuff market to presenting a significant challenge to UST, through the introduction of new "rough-cut" and "long-cut" products, through the introduction of different product packaging in the form of plastic cans with longer shelf lives, and through the introduction of price-competitive "price-value" products. These facts, if proven at trial, would tend to show the kind of "merits" competition which markets ideally provide, in which price and product innovation drive competition and provide benefits to consumers.

Conwood's proof developed in discovery, to some extent, tends to show that, in response to growth in the price-value market, UST engaged in a campaign, directed by high-level management, to "actively pursue strategies to limit the growth of the price-value market." Arguably, the strategy selected by UST management was not to compete on price (a strategy which apparently caused a stunning one-day drop in the market valuation of Philip Morris stock when it cut cigarette prices), but to limit the distribution at retail outlets of competing brands of moist snuff. This strategy, as Conwood paints it, was designed to "eliminate competitive distribution" and to seek "exclusive vending" and "vendor exclusivity."

Of course, generalized statements by corporate executives in internal documents do not by themselves constitute antitrust law violations. However, the proof which Conwood has developed through discovery could show that a highly focused UST campaign sought to have its vending racks be the exclusive outlet for all moist snuff in retail stores. The effect of such rack exclusivity would be to give UST control over the point-of-sale advertising, since all header cards would have to be displayed on UST racks. In addition, such an arrangement, in which all products from all manufacturers are dispensed from UST racks, would tend to allow UST to reduce significantly the kinds and numbers of competitive products displayed by the retailer.

Conwood's discovery proof arguably demonstrates that UST's efforts to eliminate competing racks were significantly successful. This elimination of competing racks was accomplished through a variety of sophisticated techniques, including "crew drives," the use of the alleged subterfuge of "category management" services to small retailers as a method to elbow out Conwood and other competing products, and unilateral conduct such as UST sales personnel "cleaning up" the display areas. Conwood has developed evidence that it was the practice of UST sales personnel to obtain nominal permission to remove racks from harried and inexperienced convenience store employees who might lack the knowledge or gumption to resist

the control which UST sales personnel exerted over the displays. Conwood also used explicit contractual agreements with retailers.

Conwood's proof further tends to demonstrate that the effect of these "exclusive vending" practices was to reduce the space allocated to moist snuff in retail outlets, to exclude competing advertisements at the point-of-sale, to increase slot width in the racks so as to make fewer consumer choices available, and to manage the presentation of products in the UST racks so that slow-moving UST products would "crowd out" price-value products by occupying scarce slots in the racks. In addition to an organized category management program, UST also pursued a Customer Alliance Program ("CAP") which arguably required preferred positioning for UST products and POS advertising.

The court emphasizes that it does not here find that Conwood will succeed in proving that these events occurred, or that they occurred to the extent alleged, but only that Conwood has raised sufficient factual basis for the issues to be presented at trial rather than rejected through summary judgment.

AN OVERVIEW OF THE PARTIES' ARGUMENTS

In a carefully and vigorously argued series of pleadings which focus on certain specific antitrust issues, UST asserts that Conwood has failed to make out a triable § 2 antitrust case against it. For purposes of the summary judgment motion only, UST does not challenge many of Conwood's factual predicates. UST, for example, does not contest in this motion that it possesses monopoly power, although it seriously disputes that it has acquired and maintained it willfully. (UST memorandum in support of summary judgment at p. 14.) Likewise, in its reply memorandum, UST does not contest that it has acted with the intent to eliminate as much competitive distribution as possible; that it has acted to obtain exclusive rack and rack-P.O.S. agreements with retailers; or that its conduct has made it difficult for Conwood to place its products and to increase its sales. (UST reply memorandum at pp. 5-6).

Instead of contesting directly many of the principal factual assertions, UST rather argues that, even under the best view of these facts which Conwood might prove, Conwood cannot establish either an antitrust violation or antitrust injury. UST contends that Conwood cannot establish any "exclusionary" conduct in violation of § 2 of the Sherman Act. (UST memorandum at p. 14). Rather than directly meet Conwood's factually detailed assertions of willful exercise of monopoly power, UST characterizes its practices as failing to meet a narrow test of § 2 violations. For example, UST argues that its exclusionary rack practices cannot be illegal because they do not constitute the kind of exclusive dealing which would be condemned under other sections of the antitrust laws (see memorandum in opposition at pp. 17-21), and asserts that the other misconduct is nothing more than "ordinary business practices" (UST memorandum in opposition at pp. 25-37). UST continues this line of argument in its reply memorandum, contending that Conwood's case is a fatally thin "monopoly broth" which fails to prove any independent antitrust violation (UST reply memorandum at pp. 18 et seq.).

Conwood, in response to the UST motion, has prepared a highly detailed and possibly credible factual case based on extensive discovery, both documentary and by deposition. While it remains to be seen whether Conwood's assertion of the facts will be proven persuasively at trial to the jury, its factual chronology, if true, appears to assert an abuse – a willful exercise – of monopoly power by UST.

Conwood's case centers on a variety of interrelated practices which, in its view, constitute a coordinated, effective course of action by a monopolist which already enjoys a very high market share, profit margins among the highest in American industry, and limited competition without new market entrants. Most importantly, Conwood's version of the facts, if proven, could be interpreted by the jury to constitute a serious effort by a monopolist to suppress a competitor, not through competition on price, product innovation, or other merits, but based on exclusionary practices which are uniquely available to UST because of its longstanding market

dominance. Moreover, Conwood contends, UST's practice of excluding Conwood from point-of-sale advertising is unusually effective because of the many restrictions which federal and state law place on the advertising of tobacco products; thus, restricting or eliminating point-of-sale advertising by Conwood arguably has an unusually restrictive impact on Conwood's ability to compete based on price, product innovation and design, and the like.

The court is very careful to note that it does not adopt or endorse Conwood's view of the facts. Whether Conwood can persuade a jury, after a trial with witnesses and experts, of the truth of its case theory is not for the court to say on summary judgment. The issue before the court now is whether a trial is the appropriate procedure to resolve these factually intensive and hotly disputed claims.

LEGAL STANDARDS AND ANALYSIS

Both Conwood and UST point to the same general standard to applied to § 2 claims, stemming from the venerable Grinnell decision of the Supreme Court. As the Sixth Circuit recently observed,

> The offense of monopolization under Section 2 has two elements: "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident." United States v. Grinnell Corp., 384 U.S. 563, 570-71, 86 S.Ct. 1698, 16 L.Ed.2d 778 (1966).

Re/Max International, Inc. v. Realty One, Inc., 173 F.3d 995 (6th Cir. 1999). Only the "willful acquisition or maintenance" part of the test is at issue, as UST assumes *arguendo* for summary judgment purposes that it possesses monopoly power. (UST memorandum at p. 14.)

It is the application of the Grinnell-Re/Max standard to these facts which is in dispute. UST vigorously argues that Conwood falls far short of the mark, and that its "monopoly broth" is really nothing more than "stone soup." In pressing this argument, UST repeatedly asserts that

Conwood has not proven exclusive dealing by UST, that isolated incidents of bad behavior and "dirty tricks" in handling Conwood racks are not the stuff of antitrust lawsuits, and that Conwood has pointed to nothing more than vigorous competition of the kind invited, not condemned, by the antitrust laws.

There are two shortcomings in UST's argument. First, its abstract treatise on antitrust laws sidesteps the carefully developed, thoroughly documented record which Conwood has amassed. Whether Conwood can prevail at trial on its theories is uncertain, but Conwood has marshalled a significant amount of proof that UST engaged in a concerted campaign, directed from the highest levels of UST, designed to shut Conwood out from effective competition at retail outlets through the elimination of Conwood racks, the elimination of Conwood point-of-sale advertising, all in an unusual market for tobacco products where point-of-sale is the central marketplace battleground. Second, as discussed below, UST's attempts to pick apart Conwood's arguments would have the court examine the leaves and ignore the forest, something not mandated by the antitrust laws.

"'Anticompetitive conduct' can come in too many forms, and is too dependent upon context, for any court or commentator ever to have enumerated all the varieties." Carribean Broadcasting System, Ltd. v. Cable & Wireless, 148 F.3d 1080, 1087 (D.C. Cir. 1998). Thus, UST's "deconstruction" of the Conwood claims into a series of discrete antitrust theories, which UST then individually seeks to knock down, does not compel the summary judgement dismissal of this case. Caldera , Inc. v. Microsoft Corp., Case No. 2:96-CV-645(B), 1999 WL 1067490 (D. Utah Nov. 3, 1999). Instead, the court should use as its touchstone well-accepted principles of § 2 law.

The key to the second prong of the Grinnell test is the use by a defendant of anticompetitive conduct "to foreclose competition, to gain a competitive advantage, or to destroy a competitor." Eastman Kodak Co. v. Image Technical Services, Inc., 504 U.S. 451, 482-83

(1992) (quoting United States v. Griffith, 334 U.S. 100, 107 (1948)). The Supreme Court has directed the trial courts to condemn "exclusionary" or "anticompetitive" or "predatory" conduct, *see*, Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 602 (1985); the court must distinguish the improper "exclusionary" conduct from the permitted competition by a monopolist based on "superior product" and "business acumen," as permitted by Grinnell.

The distinction between the impermissible anticompetitive conduct by a monopolist and the lawful maintenance of its market share is based on determining if the defendant "has been 'attempting to exclude rivals on some basis other than efficiency.'" Aspen, 472 U.S. at 605, (quoting R. Bork, The Antitrust Paradox 138 (1978)). The Supreme Court in Aspen went on to quote from Professors Areeda and Turner:

> Thus, 'exclusionary' comprehends at the most behavior that not only (1) tends to impair the opportunities of rivals, but also (2) either does not further competition on the merits or does so in an unnecessarily restrictive way.

III P. Areeda & D. Turner, Antitrust Law 78 (1978). An important part of the inquiry, as directed by the Eastman Kodak Court, is whether conduct which impairs a rivals' opportunities can be justified by "valid business reasons." Eastman Kodak, 504 U.S. at 483, (quoting Aspen, 472 U.S. at 605). In Eastman, the Court held that there were triable issues of monopolization where there were reasons to doubt the validity and sufficiency of the business justifications asserted for the conduct.

Here, UST does not, at the summary judgment stage of the proceedings, attempt to show conclusively that the restrictions on the use of Conwood racks and Conwood POS were justified by business reasons; rather, it argues that the restrictions could never constitute violations at all. This falls short of the proof which would be required to prevail on the § 2 claims, particularly in view of the numerous record comments from high level UST personnel which arguably show an anticompetitive intent rather than a business justification for the exclusionary POS practices.

Other circuits have focused on the issue whether the defendant's conduct served a legitimate purpose and whether it impaired the opportunity of rivals more than necessary to serve such a legitimate purpose. See, e.g., Data General Corp. v. Grumman Syst. Support Corp., 36 F. 3d 1147 (1st Cir. 1994); Instructional Syst. Devel. Corp. v. Aetna Casualty & Surety Co., 817 F.2d 639 (10th Cir. 1987).

At a minimum, these issues require the development of proof at trial, not summary disposition. While UST is correct that there is no rule which makes summary judgment improper in all circumstances in antitrust cases, their factual nuances and complexity may require a full rather than a truncated inquiry, for monopolization as well as other claims.

Recent Sixth Circuit case law demonstrates the need of the district court to apply careful restraint in using summary judgment to reject antitrust claims. In Re/Max Int'l. Inc. v. Realty One, Inc., 173 F.3d 995 (6th Cir. 1999), the court overturned a grant of summary judgment to the defendants which had been entered by the trial court.. The challenged trade practice in the Re/Max decision was significantly different from this case; the plaintiff realty firm disputed the "adverse split" policy of the defendants with respect to the division of real estate commissions between buyers' agents and sellers' agents. The lengthy opinion discusses a number of § 1 problems, but also addresses the issue whether summary judgment was appropriately entered on behalf of the defendants on plaintiff's § 2 monopolization claim. In a detailed discussion of the factors which may be used to prove the relevant geographic market and what a plaintiff must show alternatively to prove exclusion of competition in a monopolization case , the Sixth Circuit held that there was a question of fact whether there had been "actual, sustained adverse effects on competition." Id. at 1019. Similarly, the present case presents complex questions of fact, which can be resolved only through trial, as to whether the sustained effects on competition which are preliminarily suggested by plaintiff's proof in the discovery record can be proven sufficiently before a jury.

One recent decision is worth particular mention. In R.J. Reynolds Tobacco v. Philip Morris Inc., 60 F. Supp. 2d 502 (M.D.N.C. 1999), the trial court granted a motion for preliminary injunction in a case involving a challenge to a Philip Morris promotional program which gave preferred position to Philip Morris products in retail outlets. In ruling that this program likely constituted exclusionary conduct, the trial court lent significance to the advertising restrictions in the tobacco industry, which apply to moist snuff as well as to cigarettes:

> [V]isibility and advertising at the point of purchase are uniquely critical to competition in the cigarette industry as competitors lack significant alternative advertising channels to compensate for the lack of visibility at the point of purchase.

Id. at 511. Thus, other trial courts have found that point-of-sale restrictions may have an unusually strong exclusionary effect in the tobacco industry because of restrictions on broadcast media advertising.

UST also argues that summary judgment is appropriate in its favor because Conwood's case is flawed in its attempt to prove that antitrust injury flowed from the supposed violations of the Sherman Act; alternatively, it argues that the damages asserted are speculative and are not caused by the actions of UST.

This theory, like the summary judgment argument on the question whether the Sherman Act was violated, must fail because of the fact-intensive nature of the dispute at bar. Multiple issues concerning injury, damage, and causation remain for trial. Included in these topics are the issue whether the damage claimed by Conwood is caused by UST, or instead is the result of independent, uncoerced decisions by retailers; whether the damage theory of Professor Leftwich, plaintiff's expert, can withstand challenge under Daubert v. Merrill Dow Pharmaceuticals, Inc., 509 U.S. 579 (1993), or other antitrust damage law principles; whether the effects on

competition and on Conwood which plaintiff claims are the result of actions by UST at all, or other market forces; and other matters.

None of these topics is susceptible to resolution on the current record, without the testing of facts which a jury trial presents. The law in the Sixth Circuit does not require the district court to "short circuit" such a potentially complex inquiry without a trial. Plaintiff need only show an injury of the type which the antitrust laws were drafted to prevent and which flows from defendant's unlawful practices. *See, e.g.*, Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477 (1977); Arthur S. Lengenderfer, Inc. v. S.E. Johnson Co., 729 F.2d 1050 (6th Cir.1984); Chrysler Corp. v. Fedders Corp., 643 F.2d 1229 (6th Cir.), *cert. denied*, 454 U.S. 893 (1981). The court does not wish to underemphasize the burden which plaintiff must meet at trial, but only to indicate that the detailed record on discovery prevents the summary disposition of issues.

The court re-emphasizes that the questions of whether these practices took place, how extensive they were, how much they were orchestrated by top management and how much by sporadic local efforts by "rogue" sales personnel, how effective they were in restraining or eliminating competition, whether they were eagerly sought by retailers or imposed by fast-talking, experienced UST representatives on sleepy seventeen year old nighttime sales clerks – all these are issues which can be resolved only by a jury. The court does not presume to determine how they will be resolved – only that they present serious issues of material fact.

CONWOOD MOTION FOR PARTIAL SUMMARY JUDGMENT

Conwood itself has moved for partial summary judgment with respect to the issues of whether the relevant market is moist snuff in the United States, and whether UST possesses monopoly power in that market. In addition, Conwood seeks summary disposition of UST's counterclaims under the Lanham Act and state law.

Just as there are many "hotly disputed" questions of fact on the § 2 liability claims of Conwood, so too are there many "hotly disputed" questions of fact on market definition which

prevent a summary ruling. (See UST memorandum in opposition to plaintiff's motion for summary judgment at p. 3.) While UST agrees that the relevant geographic market is the entire United States (see fn. 2 at p. 2 of its memorandum in opposition), UST seriously disputes the product definition offered by Conwood. UST asserts that there are questions of fact for the jury as to whether the relevant product market is broader than Conwood asserts, perhaps including all smokeless tobacco products, such as loose leaf chewing tobacco; alternatively, UST suggests that the product market could be segmented into separate product markets for natural and flavored moist snuff.

It is undisputed that Conwood, as plaintiff, has the burden of proving market definition. Given the extensive nature of discovery and conflicting factual accounts of the marketplace, the prevalence of serious expert opinion disagreements, and the obvious factor that the court is denying UST's summary judgment motion and setting the matter for trial, it would be unwarranted (and inconsistent) for this court to rule in a summary fashion on the product market. *See* Telecomm. Tech. Servs., Inc. v. Siemens Rolm Communications, Inc., 66 F. Supp.2d 1306 (N.D.Ga. 1998). Indeed, virtually everything about this litigation is, in UST's accurate characterization, "hotly disputed," and only a trial can resolve these issues.

Finally, in light of the denial of summary judgment both on the section two liability and product market motions, there is no basis for granting summary judgment to Conwood on UST's Lanham Act and state law claims. They may indeed prove out to be minor "tag along" theories, but the court will overrule Conwood's motion and permit them to proceed to trial with the vastly more extensive antitrust issues.

Ultimately, the present issue for the court is whether it should step into this complex, extensive litigation and call it to a halt without a trial. In order to do so, the court would have to conclude that there is no dispute of *material* fact. UST's argument concedes, for summary judgment purposes only, many of the facts which Conwood would have to prove at trial, thus

nimbly taking many disputed issues out of the analysis. Instead, argues UST, taking the best version of the facts which the record might show for Conwood, there still is lacking any antitrust violation. However, this is simply too narrow a view of this dispute, and the court cannot say with certainty that no trial should take place in order to measure the extent, purpose, effect, and competitive impact of the broad exclusionary campaign which Conwood seeks to prove. Whether Conwood can carry this significant burden at trial is not for the court to say on summary judgment; however, the court concludes that on a cold summary judgment record it cannot resolve this matter fairly or within the meaning of Rule 56 and applicable case law on summary judgment practice. Likewise, the issues of product market definition cannot be determined summarily.

A trial is unavoidable; indeed, a trial is the very device which the law contemplates for the resolution of this kind of dispute.

CONCLUSION

Skillful counsel for both sides have vigorously presented the court with a broad range of briefing on critical issues in this case. While each case is unique on its facts, the factual bases asserted by Conwood here are sufficiently within the range of conduct which, if proven at trial, may form the basis for a jury determination of § 2 liability. Whether a jury, with the benefit of a full factual presentation, will assess UST's conduct as justified, vigorous competition in the marketplace, or an impermissible, unjustified series of exclusionary acts by a monopolist, is an issue which this court cannot decide on summary judgment. The case abounds with material factual issues, it presents an adequate legal foundation to withstand motion practice, and it will be judged at trial and not on briefs alone. The motions for summary judgment of both UST and Conwood are denied. (Docket #s207 & 208)

IT IS SO ORDERED.

This _____ day of February, 2000.

_____
Thomas B. Russell, Judge.

United States District Court

Copies to: Counsel of Record