

# Category management and South African Competition Law

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## 1. Introduction

Category management has become a prevalent way of conducting business in the modern world for retailers. In principle, competitors, in conjunction with the retailer, determine who gets what portion of the shelf space and position in a supermarket, usually under the leadership of a “category captain”. Indeed category management poses great opportunities for growing a category and the business of the retailer and that of the manufacturers. On the other hand, it also poses the threat of facilitating collusion among competitors and aiding dominant firms to maintain their dominance by allocating themselves the prime spots on the shelf while allocating to competitors undesirable locations on the shelf or excluding them altogether. In its ten year history, the Competition Tribunal (“the Tribunal”) has had a solitary chance to state the attitude of the South African competition authorities to category management in the case of *The Competition Commission and JT International (Pty) Ltd (“JTI”) vs British American Tobacco South Africa (“BATSA”)*.<sup>1</sup> While the Tribunal has not sought to provide a *numerus clausis* on how true category management should function, it has laid out a solid foundation for manufacturers and retailers to follow if they are to avoid violating the antitrust laws of South Africa. This paper briefly chronicles the principles of category management, the pros and cons of adopting such in relation to anti-trust, and how those principles are treated in South African Competition Law in light of the *BATSA* case. Indeed much needs to be done to ensure that while retailers and manufacturers operating in a complex business environment benefit from category management, they do so without violating the competition laws of the Republic.

## 2. Defining category management

While there are a lot of definitions on category management, the same thread runs through most of them. The Federal Trade Commission (“FTC”) explained in its *Report on Slotting Allowances* that, “[a]s the name suggests, category management is an organizational approach in which the management of a retail establishment is broken down into categories of like products. Under category management, decisions about product selection, placement, promotion and pricing are made on a category-by-category basis with an eye to maximizing the profit of the category as a whole.”<sup>2</sup> A retailer will plan its strategy on a product category level rather than on a brand-by-

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<sup>1</sup> *The Competition Commission and JT International (Pty) Ltd (“JTI”) vs British American Tobacco South Africa* Case No. 55/CR/Jun05. Hereinafter referred to as “BATSA case”

<sup>2</sup> Federal Trade Commission, Staff Report On the FTC Workshop On Slotting Allowances (Feb. 2001), available at <http://www.ftc.gov/bc/slotting/index.htm> (“FTC Report”).

brand basis.<sup>3</sup> Products are grouped into commonly known and understood categories like cigarettes, toothpaste, or shampoo and are dealt with on that basis.<sup>4</sup>

In the ordinary course of category management, a retailer will typically select one supplier in that category, usually called the “category captain”<sup>5</sup>, to take the lead role in helping the retailer to implement a category management program.<sup>6</sup> The captain then assumes some level of responsibility, subject to the retailer’s approval, for the merchandising of that aisle or portion of the store. The captain provides the retailer with overall sales and trend data, usually from Nielsen or other accredited sources, expert planning, and merchandising advice, and suggests which products to carry for most profit and how to shelve them using a “plan-o-gram”, which is a schematic or map of the shelf which visually depicts where each product in a given category should be shelved.<sup>7</sup> The category captain will also typically provide recommendations on packaging assortments, product additions or deletions, promotion types, promotion schedules, and possibly also retail prices.<sup>8</sup> The retailer’s goal is to get the best, most experienced advice available on how to compete most effectively and how to satisfy its consumers.

The category management services proffered by the category captain will necessarily cover not just the captain’s own products but those of competitors as well. Ideally, the captain only recommends but the ultimate decision to implement rests with the retailer. It is a strange phenomenon that a category captain can perform category management services for more than one retailer which stocks its own products. It is even more surprising that even if the category captain is offering a service to the retailer, usually category captains pay to be able to serve in that capacity,<sup>9</sup> and then incur all the expenses that go with the category management functions.

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<sup>3</sup> Brandon Copple, *Shelf-Determination: Under Betsy Holden, Kraft Foods is Winning the War of the Aisles*, FORBES, Apr. 15, 2002, at 130, 140.

<sup>4</sup> Leo S. Carameli, Jr *The Anti-Competitive Effects And Antitrust Implications Of Category Management And Category Captains Of Consumer Products* Chicago-Kent Law Review Vol 79:1312 at 1330.

<sup>5</sup> A category captain is a single preferred manufacturer that assumes the responsibility for the category management planning and implementation for one or more products within a category in a retail shop (See Carameli, *Ibid.* at 1315).

<sup>6</sup> K Glazer, Brian R Henry, and Jonathan Jacobson *Antitrust Implications of Category Management: Resolving the Horizontal/Vertical Characterisation Debate*, THE ANTITRUST SOURCE, July 2004

<sup>7</sup> Ted Banks, *Antitrust Liability for category Management and Other New Merchandising Techniques: Have You Updated Your Counselling?* THE ANTITRUST SOURCE, March 2003 at 3. See Carameli, *supra* note 2 at 1315.

<sup>8</sup> Glazer, *supra*, note 6 at 2

<sup>9</sup> David Merrefield, *Your Payment, My Captain?*, SUPERMARKET NEWS, June 10, 1996. BATSA was paying incentives to retailers to allow it to planogram the cigarette category and to monitor compliance with that planogram. JTI and Phillip Morris also paid incentives in certain outlets to have planogramming rights.

Category management differs from shop to shop and from product to product as the FTC summarized, “[t]he exact function performed by category captains varies widely across firms and product categories.”<sup>10</sup> While potential cost savings and informational advantages for retailers are considerable, so are the threats to antitrust.

### 3. SA Competition Law and category management

While the category management principles are highly regarded and appear to be noble, they raise various causes for concern to antitrust authorities. The FTC stated that category management could possibly lessen competition in four areas.<sup>11</sup> Firstly, the FTC stated that category management can lessen competition by placing in the hands of the category captain confidential information about rivals’ plans which can lead to the category captain thwarting the plans of its rivals or competing less much to the detriment of customers. Secondly, category management can hinder the expansion of rivals when the category captain dissuade the retailer from carrying the products or a promotion conducted by a rival; or by putting the products of competitors on unpleasant positions with limited space. Thirdly, competition can be lessened by promoting collusion among retailers by “providing a common reference for pricing, promotion, and product placement”.<sup>12</sup> Fourthly, category management can facilitate collusion among manufacturers when they are encouraged to meet and agree on a category management strategy.

In South Africa, category management can cause antitrust problems similar to the ones identified by the FTC in instances where it violates the Competition Act, of 1998, as amended (“the Act”).

#### 3.1. *Collusion among retailers or manufacturers*

Collusion between either the retailer or the manufacturers is prohibited under section 4(1) of the Act. Section 4(1) of the Act states that:

“(1) An agreement between or concerted practice by firms, or a decision by an association of firms, is prohibited if it is between parties in a horizontal relationship and if –

- (a) It has the effect of substantially preventing, or lessening, competition in a market, unless a party to the agreement, concerted practice, or decision can prove that any technological, efficiency or other pro-competitive gain resulting from it outweighs that effect; or
- (b) It involves any of the following restrictive horizontal practices:
  - (i) Directly or indirectly fixing a purchase or selling price or any other trading condition;
  - (ii) Dividing markets by allocating customers, suppliers, territories, or specific types of goods or services; or

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<sup>10</sup> *FTC Report, supra* note 2, at 48.

<sup>11</sup> *FTC Report, supra* note 2, at 50.

<sup>12</sup> *FTC Report, supra* note 2, at 52.

(iii) Collusive tendering.”

There is no need to analyse “technological, efficiency or other pro-competitive gains” that may result from violations of section 4(1)(b) of the Act as the mere occurrence of these acts establishes the illegality.<sup>13</sup> If category management agreements lead to violation of section 4(1) of the Act, the parties will be prosecuted as a cartel as envisaged by that section. If the conduct is classified under section 4(1)(a) of the Act the Tribunal will apply the rule of reason approach, but if the conduct is classified under 4(1)(b) of the Act, no rule of reason approach will be applied.

### 3.2. Abuse of dominance

Category management cases can well be prosecuted under section 8(c) and 8(d) of the Act which states that:

#### **“8. Abuse of Dominance prohibited**

It is prohibited for a dominant firm to:

- (a)
- (b)
- (c) engage in an exclusionary act, other than an act listed in paragraph (d), if the anticompetitive effect of that act outweighs its technological, efficiency or other pro-competitive gain; or
- (d) engage in any of the following exclusionary act, unless the firm concerned can show technological, efficiency or other pro-competitive gains which outweigh the anticompetitive effect of its act –
  - (i) requiring of inducing a supplier or customer to not deal with a competitor;
  - (ii) ...;
  - (iii) ...;
  - (iv) ...;
  - (v) buying up a scarce supply of intermediate goods or resources required by a competitor.”

While section 8 deals with conduct that a dominant firm is prohibited from engaging in, it is important to note that in some instances a category captain can have a market share that is less than 35% or may not have market power.<sup>14</sup> However, one can also rely on section 5 of the Act to prosecute violations of category management principles.

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<sup>13</sup> Minette Neuhoff, Marylla Govender, Martin Versfeld, Daryl Dingley *A Practical Guide to the South African Competition Act (2006)* at 63.

<sup>14</sup> Section 8 of the Act applies only to dominant firms as defined in section 7. Section 7 states that:

“A firm is dominant in a market if –

- (a) It has at least 45% of the market share;

### 3.3. Vertical agreements

Vertical agreements are governed largely by section 5(1) and (2) of the Act which states that:

- “(1) An agreement between parties in a vertical relationship is prohibited if it has the effect of substantially preventing or lessening competition in a market, unless a party to the agreement can prove that any technological, efficiency or other pro-competitive gain resulting from that agreement outweighs that effect.”
- (2) the practice of minimum resale price maintenance is prohibited”

Generally, vertical agreements are viewed as having pro-competitive effects that outweigh any potential anti-competitive effects. All agreements that do not fall under minimum resale price maintenance will be subjected to a rule of reason approach. Thus one has to prove the efficiency gains once the vertical agreement has been found to be in violation of section 5(1) of the Act. It is submitted that category management cases if properly categorised fall under section 5(1) of the Act.

### 3.4. Minimum resale price maintenance (Section 5(2) of the Act)

As stated above section 5(2) of the Act prohibits minimum resale price maintenance.<sup>15</sup> A party needs to prove that the practice of minimum resale practice is implemented; a minimum resale price is relevant; and that there were measures and mechanisms to enforce or maintain the practice of minimum resale price maintenance.<sup>16</sup> In the context of category management, minimum resale price maintenance can occur where a supplier that does not have monopoly power in a category faces a dominant retailer.<sup>17</sup> The retailer would influence the manufacturer to maintain minimum prices at competing retailers by requiring the supplier to supply goods to its competitors subject to the competitors not reselling the goods for less than an agreed price.<sup>18</sup>

### 3.5. Prosecution of BATSA

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- (b) It has at least 35%, but less than 45% of that market, unless it can show that it does not have market power; or
  - (c) It has less than 35% of that market but has market power.”

<sup>15</sup> Minimum resale price maintenance can be defined as “any attempt by an upstream supplier to control or maintain the minimum price at which the product is resold by its customer”. Neuhoff et al, *supra* note 12 at 88.

<sup>16</sup> Neuhoff, *supra* note 12, at 90.

<sup>17</sup> Carameli, *supra* note 4, at 1330.

<sup>18</sup> Carameli *supra* note 4, at 1331.

The allegations in the *BATSA* case shall be discussed in detail below though it suffices for purposes of this section to state that the *BATSA* case was prosecuted under section 8 and section 5(1) of the Act and that the Tribunal correctly categorised category management agreements. The Tribunal in the *BATSA* case, rightly concluded that properly characterised, the selling of preferential space by retailers is a form of limited exclusive.<sup>19</sup> Certainly, the rights are not exclusive as the right to manage the category is limited and secondly the exercise of that right is also limited. In the *BATSA* case the Tribunal found that the right was limited firstly by the retailers' retaining the ultimate decision to control shelves and secondly, by the requirement by shops like Pick 'n Pay that for any manufacturer to participate in retailing they need to purchase the Electronic Point Of Sale ("EPOS") data of that retailer. The right was further limited by customer demand which made it more profitable for retailers to continue stocking *BATSA* competitor brands. In its conclusions the Tribunal quoted with approval Klein and Wright who state that:

"Category management contracts, which shift control of the retailer's shelf space within a product category to a manufacturer, are another form of limited exclusive, where the manufacturer determines the quantities of other, highly demanded products to be stocked."<sup>20</sup>

In a nutshell, it is submitted that the framework for prosecuting a case concerning the violation of category management principles in South Africa can be under section(s) 4, 5 or 8 of the Act. The latter section only applies if the respondent is a dominant firm.<sup>21</sup> Under section 4 one has to prove collusion or a concerted practice. For section 5 one has to prove a vertical relationship between the parties. In all instances the agreements have to be harming antitrust save for section 4(1)(b) and section 5(2) which contain *per se* prohibitions whether or not they harm competition.

#### **4. Attitude of SA Competition Authorities to category management**

The Tribunal did not hide its disdain for retailers and manufacturers hiding behind the "noble" principles of category management to advance their selfish motives while claiming to bring benefits to the manufacturer, retailer, and ultimate consumer. Indeed that explains why manufacturers are willing to expend more resources to be category captains and why *BATSA* was strongly incentivised to "defend its market share, to advance its private interests".<sup>22</sup> The Tribunal concluded that:

"We do not then accept the view that category management is properly regarded as a selfless promotion of the category, an activity that expresses a shared interest in which the returns accrue in unspecified shares to retailers,

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<sup>19</sup> *BATSA* decision, *supra* note 1, at par 76 and fn 26.

<sup>20</sup> Benjamin Klein and Joshua D Wright *Antitrust Analysis of Category Management: Conwood v United States Tobacco* at 2.

<sup>21</sup> Section 7 of the Act states that:

<sup>22</sup> *BATSA* decision, *supra* note 1, at par 85

the consumers and all the manufacturers with all the costs borne by the category captain”.<sup>23</sup>

The Tribunal further stated that:

“In the real world of profit maximisation, category management- and, in particular, the category captaincy role – is then understood as the purchase by the category captain manufacturer of a limited exclusive designed precisely to generate private returns through preferred allocations of space and position at the POS for the brands of the purchaser *vis a vis* competitor brands. Each of the owners of the competitor brands – in this instance JTI and PMI- is also a potential purchaser of the limited exclusive”.<sup>24</sup>

The Tribunal suggested that the parties (competitors) have to share the costs of category management rather than depending on the category captain to bear all costs. However, that may have the undesired effect of facilitating collusion as competitors will be more engaged with one another trying to reach consensus on the fee that the other competitors have to pay to the category captain. The logistics and consequences of heeding the Tribunal’s suggestion to share the costs would prove more detrimental to the antitrust cause by facilitating collusion.

To prove that parties hide behind category management to advance selfish motives, the Tribunal noted that the dishonesty does not only relate to the dominant manufacturer, BATSA, but in instances where a BATSA competitor outbid BATSA it secured space in excess of its market share to the detriment of the dominant manufacturer. Retailers also had a part to play in the violation of the category management principles by BATSA as they permitted space to be allocated on the basis of the manufacturer’s market shares rather than on the basis of the market shares of the individual brands – Tribunal noted that BATSA has been the principal beneficiary of all this

The Tribunal’s concerns with category management are shared by other antitrust authorities and many scholars likewise. The Federal Trade Commission’s Commissioner Thomas Leary stated that “as an antitrust matter, it seems rather strange that you would have one company advising a store on how to handle the product of its competitors”, let alone setting prices for them.<sup>25</sup> Carameli correctly argues that the manufacturer has a vested interest to see the competitors’ products fail and its products being the chief contributors to the profits realised by the retailer.<sup>26</sup>

While the antitrust authorities are sceptical of category management, particularly its likelihood to aid collusion or dominant firms to engage in prohibited anticompetitive conduct, its proponents are adamant that it is indeed a very good way of running business and does not cause antitrust harm. The advantages proffered by the proponents of category management have been properly captured by K Glazer *et al* when they state in one of their introductory notes that:

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<sup>23</sup> BATSA decision, *supra* note 1, at par 86

<sup>24</sup> BATSA decision, *supra* note 1, at par 88

<sup>25</sup> Copple, *supra* note 3, at 136.

<sup>26</sup> Carameli, *supra* note 4, at 1316

“Category management is wonderful. It enables the retailer to take a holistic approach to an entire category of products rather than determining profits and margins on an item-by-item basis. It makes great business sense for the retailer to get expert advice from a leading supplier about the overall category. The retailer does not have the financial or personnel resources to develop expertise in dozens, if not hundreds, of separate categories. Huge efficiencies flow from that transfer of knowledge – efficiencies that redound greatly to the retailer’s, and ultimately the consumer’s benefit. Category management should be applauded, not condemned, and recognised as one of the greatest business innovations since the invention of the steam engine”.<sup>27</sup>

There is clearly no doubt about the benefits of category management to both the retailer and the manufacturer. The FTC stated in its report that category management “can produce significant efficiencies that will benefit retailers, manufacturers and consumers.”<sup>28</sup> The problem arises when category management is abused as was alleged in the case of *BATSA* or when parties use it as a platform to engage in anticompetitive behaviour. Klein and Wright vehemently argue that limited exclusives like category management have pro-competitive effects as they allow a retailer to obtain a greater rate of return on its shelf space and, as a result, antitrust authorities need not be sceptical about them.<sup>29</sup>

## 5. The *BATSA* case and category management

JTI and the Commission alleged that *BATSA* was involved in conduct aimed at excluding its competitors (including JTI) from access to the various retail channels through which cigarettes are sold to final consumers. These channels include the grocery channel (mainly Shoprite and Pick ‘n Pay); organised convenience (mainly Spar Group and Pick ‘n Pay franchise); organised forecourts (Shell, Caltex, and Engen); independent convenience stores; and HORECA venues (hotels, restaurants and cafes).

It was common cause among the parties in the *BATSA* case, as the Tribunal stated, that *BATSA* was the category captain of the cigarette category, although no retailer had formally appointed it. It was undoubtedly a dominant firm as envisaged by section 7 of the Act as it had approximately 90% of the market for the supply of manufactured cigarettes in South Africa and supplied the market with 27 different brands and 142 brand extensions.

JTI and the Commission submitted that *BATSA* deviated from the principles of category management in at least five ways.<sup>30</sup> Firstly, they alleged that *BATSA* promoted its own brands rather than the category as a whole and achieved this through paying incentives to retailers to be given preferential space allocation and positioning. Secondly, *BATSA* ‘s objective was to achieve a space allocation equivalent to its national market share in various channels instead of seeking to get a

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<sup>27</sup> Glazer, *supra* note 6, at 1.

<sup>28</sup> FTC Report, *supra* note 2, at 54.

<sup>29</sup> Klein and Wright, *supra* note 18, at 3.

<sup>30</sup> See *BATSA*, *supra* note 1, at par 64.

space allocation equivalent to sales data in the various channels, regions and stores. Thirdly, BATSA abused its plannogramming function and insisted that the positioning of opposition brands is almost always in the bottom left hand corner of the CDU. Fourthly, BATSA did not consult with other participants in the category. In addition to that, retailers abdicated responsibility for the management of the cigarette category to BATSA and failed to exercise their oversight role. Finally, BATSA secured the skewed space and position outcomes against the payment of incentives and the incentives were against the principles of category management.

The Tribunal stated that when BATSA *de facto* acquired the position of category captain with or without the requirement for it to consult its rivals it could determine the space and position allocated to its rivals in the CDU and it also controlled the secondary displays of its rivals at the point of sale. While the Tribunal expressed its scepticism to category management contracts, it held that the conduct of BATSA must not be measured against a set of “abstract, idealised, and thoroughly implausible marketing principles”.<sup>31</sup> BATSA’s conduct must be judged as a limited exclusive as BATSA’s conduct was limited. The Tribunal held that although BATSA’s conduct, as stated above, inhibited competition to a certain degree, in the market for the retailing of cigarettes, the foreclosure caused by BATSA’s conduct does not amount to abuse of dominance as it was very minimal. The Tribunal said “... not only can we not identify consumer harm or find significant foreclosure arising from BATSA’s promotional activities, we cannot even ascribe harm to *competitors* from the allegedly anti-competitive conduct.”<sup>32</sup> The Tribunal did not analyse efficiency gains as harm to competition had not been established.

In concluding that no harm to competition could be found, the Tribunal offered a variety of reasons for JTI’s travails. The Tribunal stated that the market shares of JTI and other BATSA competitors remained constant or increased during the period of BATSA’s conduct showing that the conduct had a small effect. The Tribunal also concluded that it was difficult to state categorically the reason why JTI and other BATSA competitors failed to increase their market shares substantially as the introduction of BATSA’s merchandising program coincided with the advent of the dark market. The dark market commenced with the introduction of amendments to the Tobacco Products Control Amendment Act, which prohibited above the line marketing (like print media, bill board advertising, radio, television and cinema advertising – and other forms of public sponsorship) of cigarettes. It also found that the introduction of Marlboro in the South African market accounted for some of the losses in the market shares or volumes of Camel, a JTI brand, rather than BATSA’s conduct in the market.

Though the Tribunal did not convict BATSA of violating the Act through category management agreements with retailers and the ensuing conduct, a prudent retailer and manufacturer can learn valuable lessons from the *BATSA* case with regard to category management. These lessons would help to avoid the antitrust pitfalls of category management.

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<sup>31</sup> See *BATSA* decision, *supra* note 1, at par 107 at 37.

<sup>32</sup> *BATSA* decision, *supra* note 1, par 295 at 97.

## 6. Avoiding antitrust pitfalls as a retailer

A prudent retailer or manufacturer would want to avoid the antitrust pitfalls that may arise as a result of implementing category management and still derive the benefits that category management brings. In order to do that, the retailer has to ensure that the category captain is not given the role of making the final decisions on the management program but only serves to recommend to the retailer who will take the final decision. This point was critical in the *BATSA* decision where the Tribunal concluded that *BATSA* did not have the final say in all aspects of the category as its right to organise the retail point of sale was limited by retailers' retention of ultimate control and the ability of *BATSA*'s rivals to acquire "partnership status" with the retailers.<sup>33</sup> This undoubtedly contributed to the Tribunal concluding that what *BATSA* had from retailers was a *limited exclusive*.<sup>34</sup>

A prudent retailer will also ensure that the category captain stocks a variety of rival's brands that are demanded by its customers. This tends to increase the profits for the retailer and avoids loss of customers as a result of the unavailability of brands. In the *BATSA* case the Tribunal was satisfied that although *BATSA* violated category management principles, none of the retailers considered removing *BATSA*'s rival brands as there was a lot of customer demand for those brands. In addition, customer demand compelled the retailers to retain *BATSA* competitor brands on the shelves. Klein and Wright state that when the consumer demands variety then a limited exclusive is an efficient shelf space contract.<sup>35</sup>

The safest measure that a retailer can use in allocating space will undoubtedly be to use rate of sale within a specific store. In this way a brand that is selling high volumes will be allocated corresponding space and conversely, one that is not selling so well will be allocated a smaller space corresponding with its few sales. The predicament that arises with allocating space in terms of rate of sale is that manufacturers, particularly the category captain would pay for a bigger share of space and for positioning that it might not be entitled to in terms of rate of sale. Klein and Wright argued that with no incentive payment the retailer will adopt a competitively neutral merchandising strategy but the situation is different when incentive payments come into the picture.<sup>36</sup>

Retailers need not abdicate their functions to the category captain. They have to play an active role in making final decisions pertaining to the category rather than leave the category captain to make the final decision. Although the retailers in the *BATSA* case retained ultimate control, they had by and large abdicated their responsibilities to *BATSA* and hardly exercised their powers to ensure that the cigarette category is well managed and in accordance with the agreements they had with *BATSA*. Banks states that the mistake that most retailers make is to abdicate the responsibility for a category in a store and that provides an opportunity for suppliers and the aggressive sales representatives to engage mischief.<sup>37</sup>

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<sup>33</sup> *BATSA* decision, *supra* note 1 at footnote 28.

<sup>34</sup> *BATSA* decision, *supra* note 1, at par 80

<sup>35</sup> Klein and Wright, *supra* note 18, at 47.

<sup>36</sup> Klein and Wright, *supra* note 18, at 26.

<sup>37</sup> Banks, *supra* note 7, at 3

The best form of category management would be when the retailer performs it rather than giving it to a manufacturer that has vested interests. Alternatively, experts can be engaged to perform the category management function. The disadvantage of the retailer adopting these forms of category management would undoubtedly be the cost involved and the capacity required to perform such a function for the thousands of categories within a retail shop. Retailers would be reluctant to forgo the incentive payments and incur expenses to run the category. Carameli suggests that the manufacturer can still foot the bill for category management while the retailer or an external independent expert performs the function.<sup>38</sup> In that case, there would be few antitrust problems that arise from category management. The reason why retailers may not be having capacity to conduct category management functions may be because they have not been given the opportunity to do it on their own.<sup>39</sup>

## 7. Avoiding antitrust pitfalls as a manufacturer

A prudent manufacturer will ensure that if it has category management contracts with retailers and has plans for the category of products, the plans are reviewed by the legal experts. The sales plans it intends to use that contain a category management element must strongly rely on accurate information and if it contains financial incentives, those incentives must not be such that workers will bend the rules to make the extra sale. If a company is asked about a successful sales program, it must be able to demonstrate that the program is legal and that sales people were thoroughly trained on how to implement the program properly.<sup>40</sup>

There must be a good reason why the company has adopted category management strategy. Indeed if there is a good business justification, it goes a long way in making the legal reasonableness case as well.<sup>41</sup> Thus a manufacturer's strategy must be to grow its sales and not to eliminate competitors.

A prudent manufacturer limits all communications with competitors. Direct contact with competitors to obtain information will land the manufacturer in unpleasant waters. In addition, the manufacturer needs to stay away from agreements with other suppliers. The category captain should make recommendations to the retailer and implement the retailer's decision. The retailer can use a competitor of the category

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<sup>38</sup> Carameli, *supra* note 4, at 1354. Carameli suggests that if manufacturers are afraid that their money may be misdirected by the retailer, they can provide promotional funds conditioned on category management activities.

<sup>39</sup> Robert L. Steiner, *Category Management – A Pervasive, New Vertical/ Horizontal Format*, ANTITRUST, Spring 2001 at 80.

<sup>40</sup> Banks, *supra* note 7, at 2.

<sup>41</sup> Klein and Wright, *supra* note 18, at 35 who state that "One interpretation of the *Conwood* standard is that in the absence of a business justification for the conduct at issue, alleged abuses of category management relationships will be sufficient to support a violation of Section 2 without any evidence of substantial foreclosure or anticompetitive effect". See also *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 US. 585 (1985); *Int'l Rys. Of Cent.Am. v. United Brands Co.*, 532 F.2d 231, 239-40 (2<sup>nd</sup> Cir. 1976)

captain as a “validator”, but the category captain should refrain from such communications or contact.<sup>42</sup>

The contracts must be of short duration e.g one year thus ensuring that the foreclosure resulting from the contracts is minimal and competitors are given an opportunity to actively bid for shelf space and conclude agreements with the retailer. In the R.J Reynolds<sup>43</sup> case where the plaintiff challenged a merchandising program that provided payments in proportion to shelf space allocated, the program was allowed since commitments were terminable in less than a year, and the defendant, notwithstanding a market share in excess of 50%, was found not to have foreclosed competition, due to the introduction of several new brands. The *BATSA* contracts were normally for one year duration.

## 8. Conclusion

Category management has grown tremendously in the past decade and has assisted manufacturers and retailers to better understand their customers. While it is a very useful tool of conducting business, manufacturers and retailers alike need to be wary of the antitrust pitfalls awaiting them in the performance of category management contracts. The Tribunal has made it clear that it is very sceptical of category management contracts as they raise anticompetitive concerns.

Indeed the retailers need to take an active role in decision making regarding the recommendations of the category captain. They need to ensure that the category captain is not selfishly advancing its interests to the detriment of the category as a whole by closely monitoring its activities at the point of sale and that it does not get sensitive information about its competitors from the retailer. The retailer should strive as much as possible to ensure that the planogram corroborates more closely to the rate of sale. Better still if the retailer can conduct category management on its own or use experts, it should do so, perhaps at the expense of the category captain or market participants. This would by far be the best way to proceed.

The manufacturer, on the other hand, need to ensure that it does not get involved in facilitating collusion either among retailers or manufacturers. The sales staff need to be trained to conduct their work in accordance with the company policies which should be complying with antitrust laws. The company must have good business reasons why it will be doing certain things while having agreements with short durations.

While all these are noble aspirations, the very nature of category management makes it to rely on trust both from the manufacturer and the retailer. This trust is vulnerable to abuse and hence the need to monitor each other vigilantly. Failure to do that can result in antitrust disasters that can best be avoided through preventative measures. Hence, if the retailer can, it should conduct its own category management or engage an independent expert.

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<sup>42</sup> See Banks, *supra* note 7, at 8

<sup>43</sup> *R.J. Reynolds Tobacco Co. v. Phillip Morris Inc.*, 199 F. Supp. 2d 362 (M.D.N.C. 2002)