UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

March 22, 1999

The Honorable Hamilton C. Horton, Jr.
1406 Legislative Building
Raleigh, North Carolina 27601-2808

The Honorable George W. Miller, Jr.
611 Legislative Building
Raleigh, North Carolina 27601-1096

Dear Senator Horton and Representative Miller:

The Atlanta Regional Office of the Federal Trade Commission(1) is pleased to respond to your February 4, 1999, and February 17, 1999, requests for comment on "An Act to Amend the Wine Franchise Law to Provide For Exclusive Territories" (the Bill) currently being considered by the North Carolina Legislature. The Bill would make "airtight" exclusive territorial arrangements between wineries and wholesalers in the wine industry and thus create an exemption to the antitrust laws. In addition, Representative Miller requested our views on the competitive effects of the current statute governing wine distribution agreements.(2) We believe that the Bill and the current statute may provide an unnecessary exemption to the antitrust laws that might cause adverse consequences to competition and consumers in North Carolina.

The Commission is an independent administrative agency responsible for maintaining competition and safeguarding the interests of consumers. In the course of research, investigation, and litigation of antitrust matters, the staff applies established principles and recent developments in economic theory and empirical analysis to competition issues. Upon request, the staff of the Commission also analyzes regulatory or legislative proposals that may affect competition or the efficiency of the economy.(3)

The Bill being considered would prohibit wine wholesalers from distributing any brand of wine to a retailer whose premises are outside of the wholesaler's exclusive retail territory. Under the Bill, the wholesaler and the winery would establish the wholesaler's exclusive retail sales territory. These exclusive territories may be modified once the term of an agreement between a winery and wholesaler terminates. The Bill is an amendment to the current statute governing wine distribution agreements that prohibits wineries from entering into more than one agreement with any one wholesaler for each brand of wine or beverage it offers in any territory. Possible competitive effects of the underlying statute will be discussed after the effects of the Bill are analyzed.

Exclusive Territorial Restraints between Buyers and Sellers May Have Anticompetitive Effects in Some Circumstances

Our concern with the Bill is that it could legalize some restraints that might have anticompetitive effects. Under current law, which applies to the wine industry, vertical non-price restraints, such as agreements providing for exclusive territories, are illegal if they are anticompetitive.

U.S. 36, 49 (1977). For example, exclusive territorial agreements might facilitate collusive activity and could raise competitors' costs by foreclosing or disadvantaging competing firms from obtaining the inputs -- here, wine distribution agreements -- they need to compete. Such effects could follow if there was little interbrand competition (competition among dealers for different labels and brands), and the exclusive territorial arrangements eliminated substantial intraband competition (competition among dealers of the same label or brand) that previously existed.(4)

On the other hand, exclusive territories are often pro-competitive. The anticompetitive effects noted above could be offset by the factors the Supreme Court cited in Continental T.V. For example, exclusive territories could allow manufacturers (wineries) to achieve certain efficiencies in the distribution of its products by inducing competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer.(5) Continental T.V., 433 U.S. at 55.(6)

Under the rule of reason, the outcome of the analysis of any one agreement may differ under differing circumstances. The results of the analysis also may change over time in a single geographic area as changes occur in the industry (including the number of wineries, wholesalers and retailers operating in the market), in technology, and in distribution

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1. This comment represents the views of the Atlanta Regional Office of the Federal Trade Commission, and not necessarily the views of the Commission itself.

2. N.C. Gen. Stat. Sec. 18B-1200 et seq. (1998).

3. The staff of the Commission has commented in the past on the effects of vertical restrictions on competition in the w