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September 11, 1992

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BY HAND

The Honorable Charles A. James
Acting Assistant Attorney General
Room 3103
Antitrust Division
Department of Justice
Washington, D.C. 20530

Re: Request for Business Review Letter
PRIMESOURCE Joint Venture

Dear Mr. James:

On behalf of our clients, fifteen independent wholesale distributors of lawn and garden products located throughout the country, we hereby request a statement of current enforcement intentions of the Department of Justice with respect to their proposed formation of a combined selling joint venture, to be known as PRIMESOURCE. We make this request pursuant to the procedure for issuance of business review letters set forth in 28 C.F.R. § 50.6 (1991). Based on the favorable business review letters which the Antitrust Division has issued concerning analogous joint bidding groups, the minimum potential for anticompetitive consequences, the demonstrably procompetitive features of the joint venture, and the distributors' desire to market to national accounts as soon as possible, we are hopeful that the Division can issue a favorable clearance in short order.

Overview

The fifteen independent distributors of lawn and garden products involved in the PRIMESOURCE joint venture are located in various geographic regions of the country. The majority of their sales are to local independently-owned retailers or regional mass-merchandisers. Some of these distributors also supply individual outlets of national or multi-regional mass-merchandisers situated in their areas. None of these distributors, however, is capable of supplying all outlets of such mass-merchandisers, nor does any of these distributors have

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the plans, capacity, or finances to do so in the foreseeable future.

The distributors seek to form PRIMESOURCE in order to compete more effectively in the market for distribution to mass-merchandisers. Through PRIMESOURCE, the distributors intend to combine their local wholesale sales and service capabilities for the limited purpose of dealing with mass-merchandisers on a national or multi-regional level. The distributors will continue to operate independently for the purpose of servicing their local and regional accounts.

The distributors seek to form PRIMESOURCE to respond to significant changes in the lawn and garden products industry. Traditionally, lawn and garden products have been sold through local independently-owned outlets, where local merchants, familiar with the local climate, geology, and environment, provide the appropriate level of product expertise to the consumer. Local, independently-owned wholesale distributors fit these retailers' needs as well. In recent years, however, national and regional mass-merchandisers have captured a large and growing share of the lawn and garden products market. Mass-merchandisers prefer to deal with wholesalers that can supply all of their stores, provide central pricing, ordering and billing, and otherwise streamline administration. However, they also desire distributors with local expertise.

By coordinating the sales of local distributors from different geographic markets, PRIMESOURCE can provide the mass-merchandiser with the convenience of nationwide ordering and billing and an efficient means of serving the high-volume requirements of mass-merchandisers, and yet preserve the benefits of local service.

PRIMESOURCE is not the first project in the lawn and garden products industry to combine the capacities of local distributors in order to meet the needs of national and regional retailers. We are aware of one lawn and garden products wholesaler, Central Garden and Pet Company headquartered in California, that has developed nationwide distribution capacity. Central Garden has achieved this capacity through acquisitions and affiliations with independent distributors. The independent PRIMESOURCE distributors believe they must develop similar capabilities to remain competitive and viable in this changing marketplace.

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Structure of PRIMESOURCE

PRIMESOURCE will be an association of approximately fifteen independently wholesale distributors of lawn and garden products. As noted above, these distributors do business in geographic markets throughout the country. They have limited market power in the lawn and garden products market. As a group, in 1991, PRIMESOURCE distributors accounted for only \$345 million in wholesale sales of lawn and garden products. According to a National Gardening Survey conducted by the Gallup Organization for the National Gardening Association, the lawn and garden industry had approximately \$20.7 billion in retail sales in 1990. None of the PRIMESOURCE distributors has the capacity to service a nationwide or large regional multi-retailer on its own. A list of the distributors is annexed hereto as Exhibit A.

As currently envisioned, PRIMESOURCE will be incorporated in Massachusetts, and each distributor will be an equal shareholder of the corporation. A representative of each distributor will be entitled to sit on the board of directors. The board of directors will elect an executive committee of its own members. The executive committee and the distributors will not be involved in the day-to-day management of PRIMESOURCE. Instead, day-to-day management will be delegated to officers or employees of PRIMESOURCE who have no interest in any of the distributors, are not expected to be officers or employees of any distributor, and will own no stock in PRIMESOURCE. Such PRIMESOURCE officers or employees may serve on the Board of Directors or Executive Committee.

Although the distributors will associate with one another through membership in the PRIMESOURCE joint venture, the distributors will remain independent of each other and of PRIMESOURCE. Each will continue to transact its own business and to service its customers independently. With respect to sales to mass-merchandisers, there will be clear divisions of responsibility between PRIMESOURCE and the distributors. As currently planned, these responsibilities will be allocated by a series of identical contracts between each distributor and PRIMESOURCE under which each party remains responsible for performance of its own obligations. There will be no direct contractual relationships or agreements between or among the distributors relating to PRIMESOURCE.

PRIMESOURCE will be responsible for organizing and marketing national and multi-regional sales, coordinating advertising and promotional programs with mass merchandisers, providing marketing and servicing support for the distributors, communicating

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marketing, advertising and store display information to the distributors, coordinating service agreements, negotiating orders with mass-merchandisers (as described below), and arranging for orders to be processed, shipments to be made, and invoices to be sent and collected. PRIMESOURCE may provide these services directly or through subcontractors. It is presently contemplated that PRIMESOURCE may subcontract with an unaffiliated third party or with one of its member distributors to provide the data processing and related services necessary to process orders and send invoices. PRIMESOURCE anticipates significant cost savings and efficiencies by doing so. If a particular customer were to express a preference for regional order and invoice services, PRIMESOURCE would arrange for its distributors to offer a standardized order and invoice service designed to satisfy that customer's preference. The distributors will be responsible for purchasing products from the manufacturers and delivering the products to the individual stores. The distributors will monitor inventory on the local level, assist with product display, and provide general sales support and service. Arrangements for restocking of individual stores will be made between the store and the distributor at the local level. The product restocked may be billed to the national account through PRIMESOURCE.

The distributors will continue to sell to and service their other customers independent of PRIMESOURCE, and will remain free to service a mass-merchandiser's local outlets independent of PRIMESOURCE.

Orders from National Retailers

As currently planned, in the operations of PRIMESOURCE, a single member of the distributor group, in conjunction with a PRIMESOURCE officer or employee, would do the negotiating with the mass-merchandiser. The distributors believe that distributor involvement in the negotiation of the contracts between the mass-merchandiser and PRIMESOURCE will result in efficiencies and save costs. For example, distributor participation will reduce the number of PRIMESOURCE employees needed to deal with the national accounts, will effect significant cost savings in administration and training, will reduce travel expenses by allowing a distributor geographically close to a mass-merchandiser's buying center to make sales calls, and provide the mass-merchandiser with direct access to a distributor with hands-on familiarity with products and local conditions and needs.

PRIMESOURCE would be represented in negotiations with mass-merchandisers by a representative of one of its member distributors and an unaffiliated officer or employee of

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PRIMESOURCE. Different distributors may be involved in dealings with different customers or in successive negotiations with the same account, as advisable or needed, but only one distributor representative would be involved at a time. The distributor and PRIMESOURCE representative may call on customers together or separately. To control travel expense, it is anticipated that the distributor may often call on a customer alone. The unaffiliated PRIMESOURCE representative, however, will have sole authority for communicating information about an order to the other distributors. The PRIMESOURCE representative will communicate with the distributors to determine available price and order terms. There will be no direct communication among distributors about price and order terms. Negotiations will be conducted by the designated distributor and/or the PRIMESOURCE representative based upon the information provided by the PRIMESOURCE representative. Once negotiations are complete, bid information will be submitted to the other distributors through the unaffiliated PRIMESOURCE representative. Each distributor would then determine whether to participate in supplying the mass-merchandise in its geographic region. With these precautions and the fact that PRIMESOURCE distributors operate in various geographic markets and have limited market power, no significant competitive issue is raised by participation of a distributor in the negotiation process.^{1/}

In those instances where a particular outlet of a national retailer lies within a geographic market in which more than one PRIMESOURCE distributor competes, PRIMESOURCE would select a distributor to provide sales and service to that outlet, based on the following criteria: (1) the preference of the customer; (2) prior experience with the customer; (3) the economy of servicing the customer's account; (4) the opinion of PRIMESOURCE as to the qualifications of the distributors; (5) the prior and ongoing level of service provided by each distributor to the customer; and (6) the primary servicing area of each distributor

^{1/} Cf. footnote 12 in letter from Charles F. Rule to James F. Rill, February 8, 1991, citing favorable clearance of U.S.D. Corporation joint bidding program in which distributor in region containing the national customer's headquarters conducted the negotiations with the national customer.

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and the territory to be served.^{2/} In addition, as noted above, each PRIMESOURCE distributor would remain free to negotiate and contract separately with any mass-merchandise or other retailer, whether locally or nationally (if such capacity were ever reached).

The Market for Distribution of Lawn and Garden Products

The market in which distributors and retailers sell lawn and garden products is highly fragmented. On the wholesale level, each regional or local geographic market is served, at minimum, by five distributors. The more densely populated geographic markets, usually encompassing urban areas, may be served by as many as 10 distributors. Nationally, manufacturers such as Chevron Chemical Company (Ortho Division) and Stern's Miracle-Gro Products, Inc. may do business with as many as 100 to 150 distributors. In addition, some manufacturers have the capacity to deal directly with retailers, creating additional competitive pressure at the wholesale level. On the retail level, lawn and garden products are sold in a variety of regional and local garden stores, national mass-merchandise stores, regional mass-merchandise stores, feed/seed stores, supermarket/drug stores, home center stores, mail order houses, and even at roadside stands. To a large extent, on the retail and wholesale levels, lawn and garden products sales remain "mom-and-pop" operations. In addition, at the wholesale and retail levels, capital requirements are not substantial, and barriers to entry into the business are low. Hence, lawn and garden product sellers on both levels face not only strong actual competition, but substantial potential competition.

As discussed above, on the wholesale level, there is currently one entity with the capacity to sell lawn and garden products to nationwide retailers -- Central Garden and Pet Company. Central Garden has achieved that capacity through acquisition of five independent lawn and garden product distributors in 1988, and through recent affiliations with three other distributors. As a result of this consolidation, Central Garden's sales have grown from \$25 million in 1987 to \$280 million in 1991. In June 1992, Central Garden announced a public offering of 1,700,000 shares of common stock, which we understand

^{2/} We recognize that some previous business clearance requests apparently cited customer selection as the sole criteria. We believe that employing other reasonable criteria such as those PRIMESOURCE intends to use should not affect the competitive analysis.

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may have been temporarily withdrawn, to be sold for an aggregate sum of \$20,400,000. A copy of Central Garden's prospectus for the stock offering is annexed hereto as Exhibit B.

Although Central Garden apparently is the only lawn and garden product distributor with a national distribution capacity, the increased presence of nationwide mass-merchandisers in the lawn and garden products business indicates that further forms of consolidation among distributors are likely to occur. In its prospectus, Central Garden predicts such a trend, stating: "[t]o the extent that sales of lawn and garden supplies shift from smaller more specialized nursery stores to larger regional and national chains, [Central Garden] believes that there will be a similar trend toward consolidation of distributors leading to the predominance of regional and national distributors." See Central Garden's prospectus at 21. Joint ventures such as PRIMESOURCE will help to assure that the market for lawn and garden products at the wholesale distribution level remains competitive and that small local distributors will be able to participate in it.

Effects on Competition

The PRIMESOURCE joint venture is plainly procompetitive. By centralizing their purchasing, ordering, and billing functions, national retailers will be able to realize efficiencies in obtaining their supply of lawn and garden products. Local, small distributors will realize efficiencies in distribution that might not have been realized at all. Such efficiencies should ultimately benefit the consumer, e.g., in the form of reduced costs, while concurrently maintaining the benefits of localized services. The development of PRIMESOURCE will also serve to increase competition at the wholesale distribution level, where at present there is only one national distributor of lawn and garden products. See Central Garden's prospectus at 5, 29. In fact, Central Garden states that it has taken steps to insulate itself from competition from local and regional distributors and that a joint venture such as PRIMESOURCE could expose it to additional competition. See Central Garden's prospectus at 7, 29.

There is no risk that the combination of these distributors for the limited purpose of selling to mass-merchandisers will create an unreasonable restraint of trade. The market for the sale of lawn and garden products is extremely competitive and is characterized by low barriers to entry. At the same time, the market shares represented by the PRIMESOURCE members are too limited to restrict the price, quality, or availability of

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product to the consumer. Further, there is significant bargaining power at the mass-merchandiser level.

Similar Operations Have Been Granted
Justice Department Approval

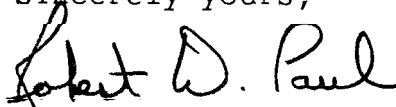
The Department of Justice has favorably reviewed several joint bidding and selling programs, including programs proposed by the Independent Drug Wholesalers Group ("IDWG") and by Affiliated Distributors ("AD"). The IDWG and AD programs are similar to the plan proposed by the PRIMESOURCE distributors. As with IDWG and AD, the PRIMESOURCE distributors are local businesses seeking to create a network for the purpose of selling to national accounts, in order to respond to buyer and competitor demands. Like the other programs, the PRIMESOURCE program will yield procompetitive effects with minimal risk of anticompetitive conduct.

Conclusion

The PRIMESOURCE distributors are eager to commence operations as soon as possible. We are available to work with you and your staff at any time to expedite this clearance. We welcome the opportunity to meet with you or your designees to address any questions raised or to provide further information.

Thank you for your attention and consideration of our request.

Sincerely yours,



Robert D. Paul

RDP/hy
Enclosures