



The Clash of Retail Titans: Winn-Dixie v. Dolgencorp

David J. Marmins

David is the co-chair of the ABA Real Estate Litigation Section land use sub-committee and co-leader of AGG's Retail industry team.

In a rare and sweeping decision with major implications in the retail industry, the Eleventh Circuit has given new life to many of Winn-Dixie's claims against three of its largest discount competitors for alleged violations of restrictive covenants in *Winn-Dixie Stores, Inc. v. Dolgencorp, LLC*, 746 F.3d 1008 (11th Cir. 2014). At the same time, it affirmed the denial of relief to Winn-Dixie on other claims. The court addressed several aspects of the commercial lease dispute, including the ability of one tenant to sue another directly for restrictive covenant violations, the definitions of common terms such as "sales area" and "groceries," and how to calculate damages for lost profits. Considering the rising percentage of discount retailers' revenue coming from consumables, this decision could reach far beyond the seemingly dense legal principles addressed in the 59-page opinion.

Winn-Dixie Sues Discount Retailer Competitors

Winn-Dixie, with about 500 grocery stores throughout the Southeast and more than \$7 billion in revenue, annually ranks in the top 25 North American food retailers. As most grocery store anchor tenants do, it typically signs lease agreements giving it exclusive rights to sell groceries in shopping centers ("exclusivity lease provisions"). But recently, it has been receiving competition from discount retailers. Over the past several years, top-100-ranked discount retailers, such as Dollar General, Dollar Tree, and Big Lots, and other smaller discount retailers have been boosting their sales primarily by increasing sales of consumable goods, such as food, paper, cleaning, and health and beauty products, as opposed to relying as heavily on durable goods. As supermarket chains and discount retailers are frequent neighbors in shopping centers, a clash seemed inevitable.

In 2011, Winn-Dixie took action to enforce its exclusivity lease provisions by suing 97 Dollar General, Dollar Tree, and Big Lots stores in the U.S. District Court for the Southern District of Florida. Winn-Dixie alleged that these stores, located in Alabama, Florida, Georgia, Louisiana, and Mississippi, violated Winn-Dixie's leases with its landlords by selling groceries in a sales area that was restricted to Winn-Dixie sales. Winn-Dixie did not sue the landlords with whom it had contracts, instead suing only its competitors. The supermarket chain alleged over \$90 million in lost profits as a result of the discount retailers infringing on its core business since 2005.

These suits were consolidated and went to trial in 2012. A federal judge denied all but very limited injunctive relief in a major victory for the discount retailers. In March, the Eleventh Circuit reversed several of the district court's findings and remanded the claims regarding 54 of the defendant retailers' stores for further proceedings while upholding the denial of relief to Winn-Dixie as to the remaining stores.

"Groceries" Means More Than Food, and "Sales Area" Means More Than Shelves

The most impactful aspect of the decision was the appellate court's disagreement with the trial court's narrow definition of "groceries" and "sales area." Neither of these key lease terms were defined in the relevant contracts. The district court found that the terms "staple or fancy groceries" and "sales area" were ambiguous, which, under applicable laws, meant they must be construed

narrowly and against the party enforcing the restrictive covenant. Therefore, the court found that “staple or fancy groceries” meant only food items, including nonalcoholic beverages, and “sales area” meant only the footprint of the display unit, excluding aisle space. These limiting definitions defeated most of the claims brought by Winn-Dixie.

The court of appeals, however, disagreed. First, it found that the terms were not ambiguous. The court looked to the *Webster’s Third New International Dictionary* definition of “groceries,” which encompassed nonfood items such as household supplies, including soap, matches, and paper napkins. The defendant retailers had argued, and the district court had agreed, that the word had evolved over time since the leases were signed, creating the ambiguity. The court of appeals, however, did the legwork of reviewing *Webster’s* definitions since 1934 and found no “material evolution of the dictionary definition of groceries over the period when the leases were signed.”

The court of appeals also found the term “sales area” sufficiently specific to avoid a narrow construction to the detriment of Winn-Dixie. The defendants argued, and the district court had agreed, that “sales area” should be limited to the physical space occupied by shelves displaying the restricted products. Winn-Dixie countered with a quote from an earlier decision addressing the same language: “Shoppers do not arrive by chopper, sending ropes down to hoist up their purchases.” See *Winn-Dixie Stores, Inc. v. 99 Cent Stuff-Trail Plaza, LLC*, 811 So. 2d 719 (Fla. Dist. Ct. App. 2002). The Eleventh Circuit agreed with Winn-Dixie that “sales area” should include the aisles and not just the shelving space.

Based on these differences of opinion with the district court, the court of appeals reversed the denial of relief to Winn-Dixie as to 41 Florida stores, 11 Alabama stores, and 2 Georgia stores, sending the cases back to the district court for a new trial applying the broader definitions of these terms. In doing so, it sent a loud message to discount retailers that they will have a harder time competing for consumable product customers with supermarkets that insist on exclusive rights to sell consumables in their shopping centers.

Landlords Are Not Necessary to Restrictive Covenant Enforcement Suits Against Cotenants

The court also found that, as to these stores, Winn-Dixie could sue the other tenants directly rather than seek relief against the landlords. The retail discounters argued that they were not parties to Winn-Dixie’s lease agreements with its landlords; therefore, Winn-Dixie should proceed against the landlords and not the other tenants. The court of appeals disagreed, finding that, because restrictive covenants are considered by state law to be real property covenants running with the land, local law applied and that, under such law in Florida, Georgia, and Alabama, the covenants were enforceable against cotenants. Further, the court rejected arguments that the landlords were indispensable parties under Federal Rule of Civil Procedure 19 because it reasoned that it was possible to “provide ‘complete relief’ among the litigants without joining the landlords” and the landlords had no rights that were impaired by the proceedings. *Winn-Dixie*, 746 F.3d at 1039, 1040.

However, that was not the case in Louisiana and Mississippi. In Louisiana, unless expressly stated otherwise, a lease contract conveys only a personal property right, not a real property right, and as a result, lease covenants do not run with the land. Therefore, the court of appeals held that “the district court did not err in concluding that Louisiana law does not recognize Winn-Dixie’s grocery exclusives as real obligations running with the land.” *Id.* at 1031. Additionally, Mississippi law “requires that privity of estate must exist between the person claiming right to enforce the covenant and the person upon whom burden of covenant is to be imposed.” *Id.* So Winn-Dixie also could not maintain an action for restrictive covenant violations in Mississippi because the defendants did not enter into contracts with Winn-Dixie.

These findings have important takeaways for retailers enforcing, or attempting to avoid, lease restrictive covenants. The most important among them is that cognizance of applicable state laws is key. Parties to lease agreements must consider the enforceability of the lease provisions against cotenants. Likewise, tenants who share space with anchors must perform due diligence to be certain of their compliance with covenants even if they are not parties to the lease agreements.

Continuing Violations of Restrictive Covenants Are Not Barred by the Statute of Limitations

The court of appeals also decided that Winn-Dixie's claims were not barred by the statute of limitations. Applicable law provided for a five-year statute of limitations for enforcing restrictive covenants. Winn-Dixie alleged violations from as far back as 2005. However, the court applied a "continuing violation" principle to allow all the claims, finding that the restrictive covenant violations were ongoing, separate acts.

Discount Retailers Hold on to Some Major Victories

The defendant retailers did salvage important victories on other grounds as to the 43 other stores. The court of appeals agreed that even if Winn-Dixie established violations of restrictive covenants, it did not establish its damages sufficiently for recovery. The district court refused to award any compensatory damages after excluding the testimony of Winn-Dixie's damages expert, Dr. Patricia Pacey, an economist. The court of appeals affirmed that Dr. Pacey did not satisfy two prongs of the *Daubert* analysis for admissibility of expert testimony because (1) her reports could not assist the trier of fact in determining a fact at issue in the case, and (2) her methodology was not sufficiently reliable.

As to the first prong, the court of appeals found that Dr. Pacey's analysis was flawed because it "measured merely the effect of the presence of a competing store, without reflecting that most of the Defendants' stores were permitted to sell some grocery products." The court of appeals affirmed the district court's finding that Dr. Pacey's reports did not assist in determining the actual damages as a result of any restrictive covenant violations; instead, it measured the overall competition between the stores. As to the second prong, the court of appeals determined that Dr. Pacey's analysis lacked the requisite specificity. It noted that "Dr. Pacey's analysis employed tools far too blunt to illuminate" the "precise" question of whether "Winn-Dixie suffered damages as a result of Defendants' sale of groceries in a larger sales area than permitted by the restrictive covenants." *Id.* at 1029. Finding that Winn-Dixie sales were lower when a Dollar Store was nearby was insufficient to answer this question.

The court of appeals also found that punitive damages were not appropriate in this case. It noted that such damages would be appropriate only if the defendants had acted in an intentional or "grossly negligent manner." *Id.* at 1035. Instead, the facts of the case showed that the "Defendants conducted themselves in accordance with a reasonable interpretation of the grocery exclusives," conduct that warranted no punitive damages.

Finally, the court of appeals also affirmed the district court's finding that Winn-Dixie could not enforce a covenant against one Dollar General store that had signed its lease prior to Winn-Dixie's lease, noting that "a party who takes an interest in property before a restriction is created, and who thus lacks notice of that limitation, is not bound by a restrictive covenant." *Id.* at 1033.

Conclusion

There is something in this case for everyone. Supermarkets now have a powerful precedent from a federal circuit of appeals that the all-important definitions of "groceries" and "sales area" are broad and encompass most consumable products and all the space in a competitor's store. Further, except in the rare states that do not allow lease agreement restrictive covenants to run with the land, anchor tenants can enforce their exclusives against competing cotenants directly. On the other hand, competitors to anchors know that proving lost profits from violations of exclusives in lease agreements is a high and difficult bar to overcome.

Authors and Contributors

David J. Marmins

Partner, Atlanta Office

404.873.8126

david.marmins@agg.com

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Atlanta Office

171 17th Street NW
Suite 2100
Atlanta, GA 30363

Washington, DC Office

1775 Pennsylvania Ave., NW,
Suite 1000
Washington, DC 20006

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