FEDERAL TRADE COMMISSION DECISIONS

FINDINGS, OPINIONS, AND ORDERS

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Took oath of office March 21, 1961

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Took oath of office December 4, 1973*

DAVID A. CLANTON, *Commissioner*
Took oath of office August 26, 1976

ROBERT PITOFSKY, *Commissioner*
Took oath of office June 29, 1978

CAROL M. THOMAS, *Secretary*
Appointed June 20, 1977

* Resigned March 9, 1979.

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FEDERAL TRADE COMMISSION DECISIONS

Findings, Opinions and Orders

IN THE MATTER OF

BANKERS LIFE AND CASUALTY COMPANY, ET AL.

Docket 9075. Interlocutory Order, Jan. 3, 1979

ORDER AFFIRMING ORDER OF ADMINISTRATIVE LAW JUDGE AMENDING COMPLAINT TO SUBSTITUTE EXECUTRIX

Administrative Law Judge Lewis F. Parker (the "ALJ") has certified for review by the Commission an order he entered on October 11, 1978, substituting as a party in this proceeding the executrix of the estate of a deceased respondent. The executrix has appealed from the ALJ's order, contending that the action against her decedent abated as a matter of law with his death and that, in any event, substitution is improper where the only relief presently sought by complaint counsel is injunctive in nature and where no determination of liability had been made by the ALJ prior to respondent's death. For the reasons set forth below, we affirm the ALJ.

Albert R. Linnick, who was named in the complaint individually and as an officer of three corporations, died in January 1978. Complaint counsel thereafter moved to amend the complaint by substituting Alice Holguin, executrix of Mr. Linnick's estate, for Mr. Linnick. Notwithstanding that the complaint itself seeks only a cease-and-desist order against Mr. Linnick, complaint counsel desire the amendment because, if they prevail herein, the complaint (Par. 25) indicates their intention to ask the Commission to file suit against respondents in U.S. District Court to obtain restitution on behalf of consumers under Section 19 of the F.T.C. Act. Accordingly, complaint counsel assert that the executrix of Mr. Linnick's estate, who is now custodian of his assets, must be substituted as a party in order to facilitate making accurate findings with respect to Mr. Linnick's conduct and in order to preserve access to his assets. To lay the foundation for such a Section 19 action, complaint counsel, on behalf of the Commission, have also filed a contingent claim against Mr. Linnick's estate in probate court.[1]

We believe, as did the ALJ, that proper disposition of this case is largely controlled by the Commission's decision in *Holiday Magic,*

[1] The executrix's arguments regarding the propriety of that claim are not properly addressed to the Commission. Hence, we do not reach them here.

Inc., 84 F.T.C. 347 (1974). In that case, following the death of a respondent, the Commission ordered substitution of his executor into the litigation, specifically holding that the Section 5 cause of action had not abated because there remained a prospect of recovery of funds from his estate for the purpose of providing redress to injured consumers. The Commission assessed the Federal Survival Statute, 28 U.S.C. 2404, and the Federal common law in *Holiday Magic,* and concluded that an equitable action seeking, in part, redress to consumers did not abate. We see no reason to disturb that holding here, and we specifically find that in the instant case, amendment of the complaint will effectuate one of the Commission's initial purposes in issuing that complaint, *viz.* to reach assets with which redress may be made to consumers, assuming liability is first established. Hence, we hold that the pending action did not abate with Mr. Linnick's death.

The executrix protests, however, that two features distinguish *Holiday Magic* from this case. First, she notes that the Section 5 complaint in *Holiday Magic,* unlike the complaint in the instant case, expressly included redress to consumers as a part of the relief sought therein. Second, she notes that the ALJ in *Holiday Magic* had already entered his initial decision finding violations on the part of respondents, whereas in the instant case the trial has not yet begun. We find these distinctions to be without significance.

With respect to the first asserted distinction, the difference between the complaints is wholly a product of an amendment to the Commission's statutory scheme and does not imply a distinction with respect to complaint counsel's ultimate objectives in the two cases. The decision in *Heater* v. *F.T.C.,* 503 F.2d 321 (9th Cir. 1974), and the 1975 amendment of the F.T.C. Act in response thereto, led to a change in Commission procedure with respect to seeking restitution for injured consumers. *Heater* held, contrary to the Commission's argument, that Section 5 of the F.T.C. Act did not include authority for complaint counsel to seek or for the Commission to order restitution to consumers. Rather, the court said, that section limited the Commission primarily to issuance of injunctive, cease-and-desist orders.[2] Thereafter, the F.T.C. Act was amended by the Congress in 1975 to add Section 19, which authorizes the Commission, *inter alia,* to file suit in U.S. District Court to seek restitution, once there is outstanding against a respondent a final Commission cease-and-desist order. In light of both the amended statutory scheme and the doubts raised by *Heater,* customary Commission practice was modi-

[2] Certain exceptions to this principle were set out by the court at 323, n.7.

fied so that redress is now ordinarily sought only in Section 19 proceedings. Current Commission practice is thus necessarily at variance with that which was extant at the time of *Holiday Magic*, the complaint in which antedated *Heater, supra.*

We therefore reject the executrix's argument. By giving notice in the complaint that restitution may be sought under Section 19, the Commission has adequately indicated that redress is an objective. It is of no moment that the Section 5 complaint itself seeks no more than a cease-and-desist order. To be sure, the Commission's interest in restraining Mr. Linnick from engaging in continued unfair or deceptive practices ended with his death, but the same cannot be said with respect to the Commission's continued interest in assets which may have been unlawfully acquired by him as a consequence of violations of the Federal Trade Commission Act. As the ALJ noted, respondent's death does not preclude findings with respect to his activities, which findings may be the predicate for a subsequent Section 19 action, notwithstanding the absence of a cease-and-desist order specifically directed against the decedent. Accordingly, the post-1975 form of actions such as this cannot be a ground for excusing Mr. Linnick's successor in interest, his estate.

With respect to the second distinction advanced by the executrix, we find the timing of issuance of the initial decision to be without importance. Concededly, the ALJ in *Holiday Magic* had already issued an initial decision finding the decedent to have violated the law, but the absence of that factor in this case cannot be controlling. Substitution of estates as parties cannot be limited solely to those estates whose decedents have already been adjudged to have violated the law, but must encompass as well the estates of those decedents who may have violated the law, and if so, whose assets may be available to provide redress to injured consumers. Thus, the amendment to the complaint merely serves to ensure that the potential Section 19 action will not be frustrated by the death of Mr. Linnick.

The executrix raises other jurisdictional, due process and collateral objections, but we find these to be without merit and to have been adequately answered by the administrative law judge. Accordingly,

It is ordered, That Order of October 11, 1978 by Administrative Law Judge Lewis F. Parker amending the complaint by substituting Alice Holguin, executrix of the estate of Albert R. Linnick, for decedent respondent Albert R. Linnick be, and it hereby is, affirmed.

IN THE MATTER OF

THE ADVERTISING CHECKING BUREAU, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2947. Complaint, January 4, 1979 — Decision, January 4, 1979

This consent order, among other things, requires a New York City administrator and auditor of cooperative advertising programs to cease designing or implementing cooperative advertising programs for their clients which limit or restrict the rights of dealers to obtain cooperative advertising allowances for merchandise they have advertised or sold at other than regular or suggested retail prices.

Appearances

For the Commission: *Jeffrey Klurfeld.*

For the respondent: *Michael W. Palmer, Baker & McKenzie,* San Francisco, Calif. and *Abner J. Golieb, Golieb & Golieb,* New York City.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, 15 U.S.C. 41, *et seq.,* and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that The Advertising Checking Bureau, Inc. has violated the provisions of Section 5 of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

PARAGRAPH 1. Respondent The Advertising Checking Bureau, Inc. ("ACB") is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its principal office and place of business at 353 Park Ave. South, New York, New York. ACB is the parent corporation of four corporate subsidiaries which respectively maintain offices in Chicago, Illinois; San Francisco, California; Memphis, Tennessee; and Columbus, Ohio.

For purposes of this complaint, the following definitions shall apply:

"Client" is defined as any person, partnership, corporation or firm which has retained The Advertising Checking Bureau, Inc. to conduct, administer or audit, or to assist in the design or implementation of, any cooperative advertising program or portion thereof.

"Dealer" is defined as any person, partnership, corporation or firm which is eligible to participate in any client's cooperative advertising program.

PAR. 2. ACB is now and has been for many years engaged in administering or auditing cooperative advertising programs on behalf of clients; it has also assisted in the design or implementation of such programs. ACB has been retained by over 400 prominent manufacturers of branded products to perform cooperative advertising services. Sales of these clients' products represent a significant volume of commerce in such industries as wearing apparel, footwear, cosmetics and watches. Annually, ACB processes over one million claims for cooperative advertising allowances that are submitted by dealers of these clients. In addition to its cooperative advertising services, ACB monitors newspapers to determine the content and frequency of advertisements disseminated by a company's dealers and those of a competitor's dealers. In this connection, it offers a tearsheet service and prepares comprehensive retail store advertising reports.

PAR. 3. The acts and practices of ACB are in or affect commerce as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. Except to the extent that competition has been hindered, frustrated, lessened and eliminated as set forth herein, every client's dealers have been and are now in substantial competition with other dealers of the same client.

PAR. 5. ACB has assisted clients to design or implement, or has itself administered or audited on behalf of clients, cooperative advertising programs or plans which limit or restrict the rights of dealers to obtain cooperative advertising credits or allowances for any merchandise which has been:

a. Sold or advertised at other than the dealers' regular selling price.

b. Sold or advertised at a sale price, at a discount price, at a promotional price, at a reduced price, at an off-price, or at a markdown.

c. Sold or advertised at less than the suggested retail price, at less than the preticketed price, or at less than any minimum resale price.

d. Sold or advertised using a price comparison.

PAR. 6. The administering or auditing by respondent, or respondent's assisting in the design or implementation of, cooperative advertising programs or plans with any of the limitations or restrictions described in Paragraph Five hereinabove has the capacity, tendency and effect of establishing, maintaining, fixing, stabilizing or otherwise illegally influencing the resale prices of dealers in clients' products, and has had and still has the capacity, tendency and effect of hindering, suppressing or eliminating competition between or among those dealers selling a client's products.

PAR. 7. The aforesaid acts and practices of respondent have injured, hindered, suppressed, lessened or eliminated actual and potential competition in a wide variety of products, and thus are to the prejudice and injury of the public; and constitute unfair methods of competition in or affecting commerce or unfair acts and practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the San Francisco Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent The Advertising Checking Bureau, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located at 353 Park Ave. South, in the City of New York, State of New York.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

For the purposes of this order, the following definitions shall apply:

"Client" is defined as any person, partnership, corporation or firm which has retained The Advertising Checking Bureau, Inc. to conduct, administer or audit, or to assist in the design or implementation of any cooperative advertising program or portion thereof.

"Dealer" is defined as any person, partnership, corporation or firm which is eligible to participate in any client's cooperative advertising program.

I

It is ordered, That respondent The Advertising Checking Bureau, Inc., a corporation, its successors and assigns, and respondent's officers, agents, representatives and employees, directly or indirectly, or through any corporation, subsidiary, division or other device, in connection with the designing, implementing, conducting, administering or auditing of any cooperative advertising program, or portion thereof, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, shall cease and desist from:

Designing, implementing, conducting, administering or auditing any plan, program or scheme, in whole or in part, in such manner as to restrict, condition or limit the right of any dealer to obtain cooperative advertising credits or allowances because of any of the following:

a. Selling or advertising any product at other than the dealer's regular selling price.

b. Selling or advertising any product at a sale price, at a discount price, at a promotional price, at a reduced price, at an off-price, or at a mark-down.

c. Selling or advertising any product at less than the suggested retail price, at less than the preticketed price, or at less than any minimum resale price.

d. Selling or advertising any product using comparative prices.

II

Any cooperative advertising plan or program which limits or restricts any dealer from obtaining cooperative advertising credits or allowances for the advertising of close-outs, irregulars or seconds shall not be deemed to violate this order.

III

It is further ordered, That respondent shall:

1. Within thirty (30) days after service of this order, mail under separate cover a copy of this order and complaint to every client whose cooperative advertising program is designed, implemented, conducted, administered or audited by respondent in such manner as to restrict, condition or limit the right of any dealer to obtain cooperative advertising credits or allowances because of any of the restrictions or limitations contained in Paragraph I hereinabove. An affidavit of mailing shall be sworn to by an official of respondent verifying that said mailing was performed.

2. Within sixty (60) days after service of this order, distribute a copy of this order to each of its operating divisions and subsidiaries and to all officers, sales personnel and auditing personnel, and secure from each such entity or person a signed statement acknowledging receipt of said order.

IV

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed changes in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of the order.

V

It is further ordered, That respondent shall, within sixty (60) days after service upon it of this order, file with the Commission a report in writing, setting forth in detail the manner and form in which it has complied with this order.

IN THE MATTER OF

KELCOR CORPORATION, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND TRUTH IN LENDING ACTS

Docket C-2948. Complaint, Jan. 8, 1979 — Decision, Jan. 8, 1979

This consent order, among other things, requires a Dallas, Tex. finance company to cease, in connection with the extension of consumer credit, failing to compute finance charges and provide relevant disclosures in the manner and form required by Federal Reserve System regulations.

Appearances

For the Commission: *Richard Gateley.*

For the respondents: *T. Kellis Dibrell, Dibrell, Dotson & Dibrell,* San Antonio, Texas.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and the Truth in Lending Act and the regulations promulgated thereunder and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Kelcor Corporation, a corporation, and C. K. Wingo, individually and as an officer of said corporation, hereinafter sometimes referred to as respondents, have violated the provisions of said Acts and the implementing regulation, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Kelcor Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Texas, with its office and principal place of business located at 907 Hedrick Building, San Antonio, Texas.

Respondent Kelcor Corporation does not engage in any consumer loan transactions itself, but operates through wholly-owned subsidiary offices located in the States of Texas, Louisiana and Oklahoma. Each subsidiary is incorporated in the respective state in which it is located under such names as Family Plan Corporation, Credit Plan Corporation, Credit Plan Corporation of Houston, Credit Plan Corporation of Corpus Christi, Credit Plan Corporation of Fort Worth, Mutual Plan Corporation, Mutual Plan of Tulsa, Inc., or Mutual Plan Corporation of Shreveport.

Respondent C. K. Wingo is an officer of the corporate respondent. He formulates, directs and controls the acts and practices of the corporate respondent and its subsidiaries, including the acts and practices hereinafter set forth. His address is the same as that of the corporate respondent.

Respondents Kelcor Corporation and C. K. Wingo formulate and control the policies, acts and practices of each of the wholly-owned subsidiaries, including the acts and practices hereinafter set forth.

The aforementioned respondents and their subsidiaries cooperate and act together in carrying out the acts and practices hereinafter set forth.

PAR. 2. Respondents, by and through their corporate subsidiary structure, are now and have been engaged in the offering to extend, and the extension of, consumer credit to the public including the financing and the granting of consumer loans.

COUNT I

Charging violations of Section 5 of the Federal Trade Commission Act and the Truth in Lending Act, the allegations of Paragraphs 1 and 2 hereof are incorporated by reference in Count I as if fully set forth verbatim.

PAR. 3. In the ordinary course and conduct of their business, as aforesaid, respondents regularly extend consumer credit, as "consumer credit" is defined in Regulation Z, the implementing regulation of the Truth in Lending Act, duly promulgated by the Board of Governors of the Federal Reserve System.

PAR. 4. Subsequent to July 1, 1969, respondents, in the ordinary course and conduct of their business, as aforesaid, have charged and are now charging a substantial number of consumers for credit life, accident and health insurance, written in connection with consumer loans.

Typical and illustrative, but not all inclusive, of the circumstances in which these insurance charges are incurred are the following:

A. Prior to presenting the loan disclosure statement to the consumer, respondents automatically include the cost of credit life and accident and health insurance on such statement, and unless the consumer specifically objects to the inclusion of the charges for such insurance, the coverage becomes part of the credit transaction.

B. In some instances, respondents' have placed a check-mark, an "x" mark or some other mark next to blank lines on the loan disclosure statement to obtain borrower's signatures for credit life and accident and health insurance and/or have placed the date in the designated position in the insurance disclosure portion of said statement without permission or authority of the consumer.

C. Respondents record the charges for credit life and accident and health insurance as disbursements and these charges become part of the amount financed, but are excluded from the finance charge in computing the annual percentage rate, as "finance charge" and "annual percentage rate" are defined in Regulation Z.

PAR. 5. By and through the acts and practices described in Paragraph 4, and others of similar import, meaning and consequence, but not specifically set forth herein, respondents, in a substantial number of instances, and particularly in connection with the sale of credit life and accident and health insurance, obtain consumers' signatures through acts and practices which operate, directly or indirectly, to defeat the elective language on the loan disclosure statements by obscuring from consumers knowledge about the option. In some instances, respondents lead consumers to believe that their signatures are necessary solely for the purpose of obtaining credit. In other instances, respondents allow consumers to sign the loan disclosure statement, electing insurance, in the mistaken belief that such insurance is required by respondents. Respondents also discourage the declination of the insurance coverage when it is questioned. These acts and practices have the effect of preventing substantial numbers of consumers from exercising their own independent, voluntary choice whether to obtain credit life and accident and health insurance.

Therefore, respondents, in a substantial number of instances, induce consumers to incur charges for credit life and accident and health insurance without said consumers making a knowing, affirmative election to have such insurance and, thereby, respondents fail to obtain from each of their customers a "specifically dated and separately signed affirmative written indication of [their] desire" to obtain such insurance, as required by Section 226.4(a)(5) of Regulation Z, in spite of the existence of language to the contrary in the loan disclosure statement.

PAR. 6. By and through the acts and practices described in Paragraphs 4 and 5 hereof, respondents fail to include the charges for credit life and accident and health insurance in the finance charge when a specific dated and separately signed affirmative written indication of the consumers desire for such insurance has not been obtained, as required by Section 226.4(a)(5) of Regulation Z, and thereby respondents:

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A. Fail to compute and disclose accurately the "finance charge" as required by Sections 226.4 and 226.8 of Regulation Z; and

B. Fail to compute and disclose accurately the "annual percentage rate" accurately to the nearest quarter of one percent, in accordance with Section 226.5, as required by Section 226.8 of Regulation Z.

PAR. 7. In the further course and conduct of their business as aforesaid and particularly in connection with their extensions of consumer credit, respondents write an insurance policy that is denominated "Cash Benefit Hospital Policy." The charge for said policy is imposed directly or indirectly by respondents as an incident to or as a condition of the extension of credit. The charges or premiums are usually paid by the consumer from the proceeds of such consumer's loans to respondent C. K. Wingo, who also does business as Eustace Insurance Agency, a sole proprietorship. Respondents do not include the charge or premium for said insurance in the finance charge.

Therefore, respondents are violating Sections 226.4 and 226.8 of Regulation Z, by failing to include the charge for the "Cash Benefit Hospital" insurance in the finance charge and by failing to specifically disclose such charge as an element of the finance charge.

PAR. 8. By and through respondents' failure to include the charge for the "Cash Benefit Hospital" insurance in the finance charge as described in Paragraph 7, respondents:

A. Fail to compute and disclose accurately the "finance charge" as required by Sections 226.4 and 226.8 of Regulation Z; and

B. Fail to compute and disclose accurately the "annual percentage rate" accurately to the nearest quarter of one percent in accordance with Section 226.5, as required by Section 226.8 of Regulation Z.

PAR. 9. Pursuant to Section 103(q) of the Truth in Lending Act, respondents' aforesaid failures to comply with the provisions of Regulation Z, constitute violations of that Act and, pursuant to Section 108(c) thereof, respondents have thereby violated and are violating the Federal Trade Commission Act.

COUNT II

Charging violations of Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs 1 and 2 hereof are incorporated by reference in Count II as if fully set forth verbatim.

PAR. 10. In the course and conduct of their aforesaid business, respondents now cause and have caused, monies, contracts, business forms and other commercial paper and printed materials in connection with consumer financing and the granting of consumer loans to be sent by United States mail from respondents' principal place of business in the State of Texas to their subsidiary corporations located in various other States of the United States, and maintain and at all times have maintained a substantial course of trade in services in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 11. In a substantial number of instances, respondents charge consumers for household goods-fire insurance written in connection with consumer loans. Typical and illustrative, but not all inclusive of the circumstances in which such charges are incurred are the following:

A. Prior to presenting the loan disclosure statement to the consumer, respondents' include the charge for household goods–fire insurance in the amount financed. Unless the consumer specifically objects to the inclusion of the charges for such insurance, the coverage becomes part of the credit transaction.

B. Respondents do not provide a place on the loan disclosure statement for the consumer to indicate his desire to obtain the household goods–fire insurance from or through respondents.

C. Respondents represent, directly or by implication, that the consumer must obtain household goods–fire insurance from or through respondents.

D. Respondents fail to disclose the cost of such insurance clearly and conspicuously in conjunction with the insurance disclosure portion in their loan disclosure statement.

PAR. 12. By and through the acts and practices described in Paragraph 11, and others of similar import, meaning and consequence but not specifically set forth herein, respondents, in a substantial number of instances, lead consumers to believe that household goods-fire insurance must be purchased from or through respondents or that such insurance is an intregal part of the entire agreement, not necessitating a separate decision, despite language to the contrary in the loan disclosure statement. These practices have the effect of preventing substantial numbers of consumers from exercising their own independent, voluntary choice whether to obtain household goods-fire insurance through respondents or whether to obtain it through other agents.

Therefore, the acts and practices set forth in Paragraph 10 are false, misleading, deceptive and unfair and a violation of Section 5 of the Federal Trade Commission Act.

PAR. 13. In the course and conduct of their business, and at all times mentioned herein, respondents have been in substantial competition, in or affecting commerce, with corporations, firms and individuals in the sale of services of the same general kind and nature as those sold by respondents.

PAR. 14. The use by respondents of the aforesaid unfair, false, misleading or deceptive acts and practices, and their failure to disclose certain facts, as alleged above, has had and now has the capacity and tendency to mislead members of the public into the erroneous and mistaken belief that those statements and representations were and are true and complete, and into the purchase of and payment for household goods-fire insurance written in connection with consumer loans by reasons of said erroneous and mistaken beliefs.

PAR. 15. The aforesaid acts and practices of respondents, as herein alleged, are all to the prejudice and injury of the public and of respondents' competitors and constitute unfair methods of competition in or affecting commerce and unfair and deceptive acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof and the respondents having been furnished thereafter with a copy of a draft of complaint which the Dallas Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violations of the Truth in Lending Act and the regulation promulgated thereunder and violations of the Federal Trade Commission Act; and

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by respondents of all jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for the settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated said Acts, and that complaint should issue stating its charges in that respect and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure described in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jursidictional findings, and enters the following order:

1. Respondent Kelcor Corporation is a corporation organized, existing and doing business under an by virtue of the laws of the State of Texas, with its office and principal place of business located at 907 Hedrick Building, San Antonio, Texas.

Respondent Kelcor Corporation does not engage in any consumer loan transactions itself, but operates through wholly-owned subsidiary offices located in the States of Texas, Louisiana and Oklahoma. Each subsidiary is incorporated in the respective state in which it is located under such names as Family Plan Corporation, Credit Plan Corporation, Credit Plan Corporation of Houston, Credit Plan Corporation of Corpus Christi, Credit Plan Corporation of Fort Worth, Mutual Plan Corporation, Mutual Plan of Tulsa, Inc., or Mutual Plan Corporation of Shreveport.

Respondent C. K. Wingo is an officer of the corporate respondent. He formulates, directs and controls the acts and practices of the corporate respondent and its subsidiaries and his address is the same as that of the corporate respondent.

Respondents Kelcor Corporation and C. K. Wingo formulates, directs and controls the policies, acts and practices of each of the wholly-owned subsidiaries.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

Order

I

It is ordered, That respondents Kelcor Corporation, a corporation, its successors and assigns, and its officers, and C. K. Wingo, individually and as an officer of said corporation, and respondents' agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with the granting of consumer loans or with any other extension of consumer credit or advertisement to aid, promote or assist directly or indirectly any extension of consumer credit, as "consumer credit" and "advertisement" are defined in Regulation Z (12 C.F.R. 226) of the Truth in Lending Act (Pub. Law 90–321, 15 U.S.C. 1601, *et seq.*), do forthwith cease and desist from:

1. Failing to include and to itemize in the Truth in Lending disclosure statement the amount of charges for credit life, accident, health or loss of income insurance as part of the finance charge, unless the amount of such charges is excluded from the finance charge because of the option available pursuant to Section 226.4(a)(5) of Regulation Z and disclosures are made in accordance with paragraph 2 following. In the event such charges are included in the finance charge, respondents shall make the following disclosure clearly and conspicuously on the disclosure statement on the front side of the page and immediately above or adjacent to the blank for the consumer's signature which consummates the loan transaction. Said disclosure shall be in the following form and set off from the text of the instrument by a black border:

NOTICE

The charges for credit life, accident, health or loss of income insurance [as applicable] are included in the finance charge. As a result, the annual percentage rate for your loan is higher than it would be if such charges were not included.

2. Offering or presenting to any consumer optional credit life, accident, health or loss of income insurance where respondents seek to invoke the elections provided by Section 226.4(a)(5) of Regulation Z unless respondents:

A. Read to each consumer at the time of the first personal meeting the following statement. A copy of the statement shall be given to the consumer simultaneously therewith. It shall be printed in a clear and conspicuous manner in 12-point bold-faced type on one side of a single sheet of paper which does not contain the consumer credit agreement:

NOTICE

Credit life, accident, health or loss of income insurance is entirely optional. You are not required to buy any such insurance to obtain a loan and your choice regarding insurance coverage will not be considered in our decision on approving a loan.

B. Retain a copy of the statement, signed and dated by the consumer and the employee who reads the statement to the consumer, for a period of two (2) years from the date shown thereon and provide a copy of said executed statement to the consumer at the time of the first personal meeting.

C. Present to the consumer as the first document at the time of consummating the loan or other consumer credit transaction a separate, written insurance authorization form which sets forth clearly and conspicuously that:

(i) The consumer has received credit approval up to a specified amount;

(ii) The consumer's decision with regard to the insurance available through respondents is not considered in granting the credit;

(iii) Insurance is optional and is not required to obtain the loan;

(iv) The amount of the total charge for credit life insurance, the total charge for credit accident and health insurance and/or the total charge for loss of income insurance along with the net proceeds payable in each instance;

(v) The monthly payments which would result from the consumer's election to take the loan, set forth in the following order from left to right across the document: (1) without credit life, accident and health or loss of income insurance, (2) with credit life insurance only, (3) with credit accident and health insurance only, (4) with loss of income insurance only and (5) with credit life, accident and health and loss of income insurance; and, if applicable, (6) with other available forms of credit insurance; and

(vi) A blank signature and date line for each option set forth in (v) above for the consumer to indicate his election.

(vii) The borrower authorizes respondents on behalf of the borrower to pay the insurance premiums to the insurance company for such personal insurance which has been chosen.

D. Make the disclosures in the manner and form required by sub-paragraph C above on a separate document which contains no other printed or written material. The disclosures required by sub-paragraphs (i), (ii) and (iii) above shall not be smaller than 12-point type. A form in conformance with Attachment A herein will be considered as in compliance with disclosure provisions of this sub-paragraph and sub-paragraph C. Respondent shall provide the consumer with an executed copy of the said insurance authorization form at the time a loan or other consumer credit transaction is consummated. Respondents shall retain a copy of said form for a period of two (2) years following its execution and make such copy available to the Federal Trade Commission or its staff for inspection and copying on request.

E. Cease and desist from:

(i) Failing to leave the Truth in Lending disclosure statement blank as to the cost of credit life, accident, health or loss of income insurance and all other information or amounts which are affected by the election or declination of insurance until the consumer has signed the written insurance authorization form required by sub-paragraph C above electing the insurance coverage.

(ii) Making any marks or otherwise instructing a consumer where to sign or date the separate insurance authorization form required by sub-paragraph C above in advance of the consumer's free and independent choice for such insurance.

(iii) Representing, by any means, that credit life, accident, health or loss of income insurance is required to obtain an extension of credit from respondents.

(iv) Discouraging by any means the declination of credit life, accident, health or loss of income insurance.

3. Offering or presenting to any consumer the "Cash Benefit Hospital Policy" or any insurance other than credit life, accident, health, loss of income or property insurance without including the charge therefor in the finance charge.

4. Failing to tell every consumer the purpose(s) of each signature requested by respondents on any document relating to a consumer credit transaction.

5. Supplying, orally or in writing, any information to a consumer which misleads or confuses the consumer, or which contradicts, obscures or detracts from the information to be disclosed by Section I of this order or by Regulation Z.

6. Failing to compute and disclose accurately the finance charge, as required by Sections 226.4 and 226.8 of Regulation Z.

7. Failing to compute and disclose accurately the annual percentage rate to the nearest quarter of one percent as required by Sections 226.5 and 226.8 of Regulation Z.

8. Failing in any consumer credit transaction or advertisement to make all disclosures, determined in accordance with Sections 226.4 and 226.5 of Regulation Z, in the manner, form and amount required by Sections 226.6, 226.7, 226.8 and 226.10 of Regulation Z.

II

It is further ordered, That respondents Kelcor Corporation, a corporation, its successors and assigns, and its officers, and C. K. Wingo, individually and as an officer of said corporation, and respondents' agents, representatives and employees, directly or through any corporation, subsidiary, division or other device in connection with the advertising, offering for sale, sale or distribution of household goods-fire insurance or other property insurance incident to any extension of consumer credit in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

1. Failing to include and to itemize the amount of charges for household goods-fire insurance or other property insurance as part of the finance charge, unless the amount of such premiums or

charges are excluded from the finance charge as allowed by Section 226.4(a)(6) of Regulation Z. In the event such insurance charges are included in the finance charge, respondents shall make the following disclosure clearly and conspicuously on the side of the page and above or adjacent to the place for the consumer's signature. Said disclosure shall be in the following form and set off from the text of the instrument by a black border:

NOTICE

The charges for household goods - fire insurance or other property insurance are included in the finance charge. As a result, the annual percentage rate for your loan is higher than it would be if such charges were not included.

2. Offering or presenting to any consumer household goods-fire insurance or other property insurance unless respondents:

A. Present to the consumer at the time of consummating the loan or other consumer credit transaction a separate, written insurance authorization form which sets forth clearly and conspicuously that:

(i) The consumer's decision of whether to purchase insurance from or through respondents is or is not considered [as applicable] in granting the credit;

(ii) Household goods-fire insurance or other property insurance is or is not required [as applicable] to obtain the loan;

(iii) The total premium for household goods-fire insurance or any other property insurance along with the net proceeds payable;

(iv) The consumer may or may not elect [as applicable] to purchase property insurance through or from respondents;

(v) The consumer may or may not elect [as applicable] to furnish respondents with an existing property insurance policy or one purchased through a third party together with a loss payable clause or endorsement naming respondents as loss payee;

(vi) The consumer has ten (10) days from the date of disclosure to exercise the election, if any, disclosed in accordance with sub-paragraphs 2(A)(iv) and 2(A)(v) of Section II of this order;

(vii) In the event such insurance is not required, a signature and date line for the consumer to indicate his election; and

(viii) In the event such insurance is required, a signature and date line for the consumer to indicate that he has read the disclosures.

B. Make the disclosures in the manner and form required by sub-paragraph A above on a separate document which contains no other printed or written material. The said disclosures shall not be smaller than 12-point type. Disclosures given in the form of Attachment B herein will be considered as in compliance with the disclosure provisions of this sub-paragraph and sub-paragraph A. Respondents shall provide the consumer with an executed copy of the said insurance authorization form at the time the loan or other consumer credit transaction is consummated. Respondents shall retain a copy of said form for a period of two (2) years from the date shown thereon and make such copy available to the Federal Trade Commission or its staff for inspection and copying upon request.

C. In the event that household goods-fire insurance is optional, cease and desist from:

(i) Making any marks or otherwise instructing a consumer where to sign or date the separate insurance authorization form required by sub-paragraph A above in advance of the consumer's free and independent choice for such insurance.

(ii) Representing, by any means, that household goods-fire insurance or any other property insurance is required to obtain an extension of credit from respondents.

(iii) Discouraging by any means the declination of household goods-fire insurance or other property insurance.

3. Failing to tell every customer the purpose(s) of each signature requested by respondents on any document relating to a consumer credit transaction.

4. Supplying, orally or in writing, any information to a consumer which misleads or confuses the consumer, or which contradicts, obscures or detracts from the information required to be given to a consumer pursuant to Section II of this order.

III

It is further ordered, That whenever a credit transaction is principally conducted in a language other than English, *e.g.,* Spanish, that any disclosures required by paragraphs 1 or 2 of Sections I and II of this order be given in the form and manner prescribed therein but in the same language as that principally used in the credit transaction with the consumer.

It is further ordered, That respondents deliver a copy of this order to cease and desist to all present and future personnel of the corporate respondent at its general offices in San Antonio and in each of its subsidiary offices engaged in any extension of consumer credit, and that respondents secure a signed statement acknowledging receipt of said copy of this order from each such person and retain said statement for a period of not less than two (2) years from the date of execution.

It is further ordered, That the corporate respondent notify the Commission within thirty (30) days of any change in the corporate respondent which may affect compliance obligations with regard to the extension of consumer credit arising out of this order, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of this order.

It is further ordered, That the individual respondent named herein promptly notify the Commission of the discontinuance of his employment with Kelcor Corporation or its subsidiaries, and of his affiliation with another business or employment. In addition, the individual respondent named herein shall promptly notify the Commission of his affiliation with another business or employment whose principal activities include the granting of consumer loans or any extension of consumer credit or advertising to aid, promote or assist directly or indirectly any extension of consumer credit or his affiliation with another business or employment in which his own duties and responsibilities involve the granting of consumer loans or any extension of consumer credit or advertising to aid, promote or assist directly or indirectly any extension of consumer credit. Such notice shall include respondent's current business address and a statement as to the nature of the business or employment in which he is engaged, as well as a description of his duties and responsibilities.

It is further ordered, That the respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

ATTACHMENT A

PERSONAL CREDIT INSURANCE AUTHORIZATION

YOUR LOAN [OTHER EXTENSION OF CREDIT] HAS BEEN APPROVED IN THE AMOUNT OF ______________.

CREDIT LIFE OR CREDIT ACCIDIENT & HEALTH INSURANCE IS NOT REQUIRED IN CONNECTION WITH THIS EXTENSION OF CREDIT TO YOU AND YOUR DECISION WITH REGARD TO THE PERSONAL INSURANCE WILL NOT AFFECT THE TOTAL AMOUNT OF CREDIT WHICH HAS ALREADY BEEN APPROVED FOR YOU.

IF YOU ELECT CREDIT INSURANCE THESE PREMIUMS WILL BE DEDUCTED FROM THE PROCEEDS OF YOUR LOAN AND ADDED TO THE AMOUNT FINANCED.

Credit Life	$_____	(For term of transaction)
NET PROCEEDS	$_____	
Credit Accident & Health (A&H)	$_____	(For term of transaction)
NET PROCEEDS	$_____	

The above disclosure of personal insurance has been read to me and I have received a fully completed and executed copy of this form. I have reviewed the monthly repayment options set forth below and understand that if I choose a repayment option that includes any of the insurance coverages I am authorizing the lender to pay the insurance premiums on my behalf. I have voluntarily chosen the following repayment option:

Option 1	Option 2	Option 3	Option 4
Monthly Payment Without Personal Credit Insurance	Monthly Payment With Credit Life Only	Monthly Payment With Credit A & H Only	Monthly Payment With Credit Life and A & H
$______	$______	$______	$______
No. of months ____	No. of months ____	No. of months ____	No. of months ____
______ (Borrower)	______ (Insured Borrower)	______ (Insured Borrower)	______ (Insured Borrower)
______ (Borrower)	______ (Borrower)	______ (Borrower)	______ (Borrower)
______ (Date)	______ (Date)	______ (Date)	______ (Date)

ATTACHMENT B

PROPERTY INSURANCE AUTHORIZATION

YOUR LOAN [OTHER EXTENSION OF CREDIT] HAS BEEN APPROVED.

PROPERTY INSURANCE IS REQUIRED TO KEEP THE COLLATERAL OF THE LENDER INSURED AGAINST LOSS OR DAMAGE. YOU MAY ELECT TO PURCHASE THE REQUIRED PROPERTY INSURANCE THROUGH LENDER OR FURNISH LENDER WITH A COPY OF ANOTHER POLICY WHICH YOU MAY HAVE CURRENTLY OR WHICH YOU CAN PURCHASE ELSEWHERE THROUGH ANOTHER PERSON, TOGETHER WITH A LOSS PAYABLE CLAUSE OR ENDORSEMENT NAMING LENDER AS LOSS PAYEE WITHIN TEN (10) DAYS.

IF YOU ELECT PROPERTY INSURANCE FROM THE LENDER, THESE PREMIUMS WILL BE DEDUCTED FROM THE PROCEEDS OF YOUR LOAN AND ADDED TO THE AMOUNT FINANCED.

Auto Insurance Premium	$______ (For One Year)
Fire Insurance Premium	$______ (For Term of Transaction) [As applicable]
NET PROCEEDS	$______

THE ABOVE DISCLOSURE OF PROPERTY INSURANCE HAS BEEN READ BY ME AND I HAVE RECEIVED A FULLY COMPLETED AND EXECUTED COPY OF THIS FORM.

______ LENDER

______ BORROWER

______ DATE

IN THE MATTER OF

NEW JERSEY PEST CONTROL ASSOCIATION, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2950. Complaint, Jan. 8, 1979 — Decision, Jan. 8, 1979

This consent order, among other things, requires a West Orange, N.J. trade association, representing a number of dealers and suppliers of pest control goods and services, to cease denying membership to bona fide dealers and suppliers; establishing or maintaining prices or conditions of sale for goods and services; interfering with advertising media; or attempting by any other means to fix prices and eliminate competition in relevant markets. The association is further required to eliminate timely from its charter and by-laws any provision which is contrary to the terms of the order, and to maintain specified records for a three-year period.

Appearances

For the Commission: *Herbert S. Forsmith.*

For the respondent: *John F. Doly,* West Orange, N.J., *Edward J. Hobbie, Chamberlin & Hobbie,* Hillside, N.J. and *Arthur L. Herold, Webster & Chamberlain,* Washington, D.C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, (15 U.S.C. 41, *et seq.*) and by virtue of the authority vested in it by said Act, the Federal Trade Commission having reason to believe that the party listed in the caption hereof, New Jersey Pest Control Association, Inc., a corporation, and more particularly described and referred to hereinafter as respondent, has violated the provisions of Section 5 of the Federal Trade Commission Act, as amended, and it appearing to the Commission that a proceeding by it in respect thereof would be in the interest of the public, hereby issues its complaint stating its charges as follows:

PARAGRAPH 1. Respondent New Jersey Pest Control Association, Inc. is a non-profit incorporated trade association whose members are engaged in business for profit. It was organized in 1943, and exists and does business under and by virtue of the laws of the State of New Jersey. Respondent maintains its office and principal place of business at 475 Prospect Ave., West Orange, New Jersey.

The respondent is composed of approximately one hundred pest control applicators located within and without the State of New Jersey serving the New Jersey residential and commercial markets for pest control goods and services designed to eliminate insects and rodents, and approximately twenty suppliers to the trade located in New Jersey and various other States of the United States.

Its members, comprising at least one fourth of pest control companies engaged in the business of pest control application in New Jersey, realized at least 50 percent of the state's approximately fifteen million dollars of trade in the pest control industry during the year 1975.

PAR. 2. The affairs of respondent association are managed by a Board of Directors and an Executive Board of Officers which are elected by a senior class of respondent's membership designated as the Active Membership. Admission to the Active Membership is restricted to pest control operators who have served a prolonged probationary period in respondent association, and who have satisfied the Active Membership that they are responsible full-service pest control operators.

Only those belonging to such Active Membership are permitted to vote upon respondent's business, to serve as respondent's officers or committee chairmen, or to advertise and disclose to those outside of the association the fact of their membership in respondent.

PAR. 3. Respondent is a well-known and well-advertised association as a result of its active and varied programs designed to provide technical training and information to its membership, and to promote such membership's reputation and financial interests.

By virtue of a number of circumstances, including action on the part of respondent association to that end, there exists a preference on the part of purchasers and prospective purchasers for members of the respondent as pest control dealers and applicators, and on the part of private and governmental persons and organizations frequently called upon to recommend pest control dealers and applicators, or to establish or approve particular pest control methods or procedures.

It therefore confers special benefits and is of substantial competitive importance to a dealer in pest control goods or services to belong to respondent association, and to be able to advertise and disclose such membership.

PAR. 4. Most of the members of the respondent purchase equipment and supplies for resale or use directly from manufacturers and distributors thereof located in various other states, and said manufacturers and distributors ship said products, when so purchased, from their respective places of business to said members in states other than the state of manufacture or storage. Further, many of the members of the respondent maintain their principal places of business in states other than the State of New Jersey, and many of such members are engaged in the business of selling and supplying pest control materials to customers located in states other than the state in which such members are located, or without the State of New Jersey. As a result of the aforesaid transactions, and by virtue of respondent association's representation of its members, and promotion of their business, respondent association and its membership have been and are now engaged in a pattern, course of dealing, and substantial volume of trade in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, as amended, in pest control products and services between the said members of the respondent trade association, and the purchasers of pest control goods and services located throughout several States of the United States.

PAR. 5. The pest control dealers and applicators holding membership in the respondent are in substantial competition with one another and with other members of the industry in the sale of pest control goods and services, in or affecting commerce, except insofar as that competition has been hindered, lessened, restricted and eliminated by the unfair methods of competition and unfair practices hereinafter set forth.

PAR. 6. For many years last past, and continuing in the present time, respondent has planned, adopted, placed in effect, and carried out, policies having the purpose, tendency and effect of hindering, frustrating, restraining, suppressing and eliminating competition in the offering for sale and sale of pest control goods and services in or affecting commerce.

Pursuant to and in furtherance of the above policies respondent has, alone and by means of agreements, understandings, and combinations and conspiracies with certain of its members, and with others, engaged in the following acts and practices:

(a) Denied, and restricted membership in respondent association by means of certain arbitrary rules and standards, and thereby refused substantial competitive advantages of such membership to bona fide dealers in pest control goods and services with which members of respondent association were not willing to compete upon an equal basis. Included among the reasons for such denials and restrictions are the following:

(1) a dealer cuts prices, or offers, advertises or charges low prices or underbids its competition;

(2) a bona fide dealer is in the pest control business on a part-time basis;

(3) a bona fide dealer is in the pest control business on less than a year-round basis;

(4) a bona fide dealer is engaged in another business or occupation as well as being in the pest control business;

(5) a bona fide dealer does not perform services designed to control both insects and rodents;

(6) a bona fide dealer has not been engaged in the pest control business, or has not served as a limited member of respondent for a requisite length of time;

(7) a bona fide dealer offers terms or conditions of sale, such as warranties, not approved by respondent association.

(b) Conspired and combined to maintain price floors, minimum charges and higher prices for pest control goods and services; to prevent through intimidation and other means, price cutting and discounting in connection with the offering and sale of pest control goods or services; and to cause the reporting to respondent association of dealers in pest control goods or services believed to be offering discounts or lower prices than those approved by respondent association or certain of its members.

(c) Denied and attempted to deny full access to advertising media to non-members and certain members of the respondent by prevailing upon such media to refuse, condition, qualify or change advertising placed or sought to be placed for reasons, among others, that such advertising contains prices, terms or conditions of sale not approved by respondent association or its members.

PAR. 7. The acts, practices and methods of competition engaged in, followed, pursued or adopted, by respondent, as hereinabove alleged, are unfair, and to the prejudice of the public because they have the purpose or tend to have the effect of hindering, lessening and restraining competition in the sale of pest control goods and services between and among pest control dealers; restrain competition between and among non-members and members of respondent trade association; raise barriers to entry of new competition in the sale of pest control goods and services; and limit and restrict channels of distribution of pest control goods and services.

Said acts, practices and methods of competition constitute unreasonable restraints of trade and unfair methods of competition in or affecting commerce within the intent and meaning of Section 5 of the Federal Trade Commission Act, as amended.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the New York Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent New Jersey Pest Control Association, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its principal office and place of business located at 475 Prospect Ave., West Orange, New Jersey.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

It is ordered, That respondent New Jersey Pest Control Association, Inc., a non-profit corporation, and its officers, directors, agents, representatives, employees, successors and assigns, directly or indirectly, through any corporation, subsidiary, division, committee or other device, in connection with respondent association's business, or with the offering for sale, sale, distribution or promotion of pest control goods or services, in or affecting commerce, as commerce is

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defined in the Federal Trade Commission Act, as amended, shall forthwith cease and desist from entering into, cooperating in, or carrying out any agreement, understanding or combination, express or implied, or unilaterally to do, adopt or perform any of the following acts, policies or practices:

1. Failing to grant equal, uniform and nondiscriminatory membership upon written application therefor, to any dealer in pest control goods or services actually doing business within the territorial limits served by respondent association; except that this order paragraph shall not prohibit the respondent from denying membership to an applicant who has not complied with state or federal laws pertaining to qualification for the practice of pest control within the territorial limits served by respondent association.

2. Fixing, maintaining, establishing, setting, or attempting to fix, maintain, establish or set, prices, terms, or conditions of sale or price floors or minimum charges to consumers for pest control goods or services.

3. Eliminating or attempting to eliminate the granting or offering of discounts, or the advertisement of prices or discounts.

4. Requesting, suggesting, encouraging, requiring or demanding the reporting to respondent of dealers believed to be engaged in price cutting, or believed to be engaged in the granting, offering or advertisement of price cuts or discounts.

5. Requesting, suggesting, requiring, demanding or prevailing upon any advertising medium to refuse, condition, qualify or change advertising placed or sought to be placed by any dealer in pest control goods or services, because such dealer is not a member of respondent, or because such advertising contains representations relating to prices, terms or conditions of sale not approved by respondent or any member of the respondent; except that this paragraph shall not be construed in such a way as to prohibit the respondent from informing advertising media that a firm is representing itself to be a member of respondent or is using respondent's logo when, in fact, such firm is not a member of respondent.

6. Restricting or preventing, or attempting to restrict or prevent, dealers in pest control goods or services from carrying on lawful courses of action, and engaging in trade and commerce by lawful methods of their own choosing.

7. Eliminating or attempting to eliminate competition between or among dealers in pest control goods and services.

8. Requiring or requesting members of, or applicants for, membership in respondent to submit or disclose prior, current or planned advertising, or prior, current or planned prices.

It is further ordered, That respondent shall within thirty (30) days of the effective date of this order:

(1) Advise in writing and by mail all dealers in pest control services discovered through the best efforts of respondent to be doing business within the territorial limits served by respondent, that all dealers so engaged, and complying with state and federal laws pertaining to qualification for engaging in pest control services within such territorial limits, are eligible to join respondent association on equal, uniform and non-discriminatory terms.

(2) Mail a copy of this order to each dealer in pest control services discovered through the best efforts of respondent to be doing business within the territorial limits served by respondent.

It is further ordered, That immediately upon completion of the above mailings, respondent obtain from the person actually performing the required mailing of each notice and order, an affidavit verifying the mailing of each such document, and specifying the particular business entity and address to which each such document had been mailed.

It is further ordered, That respondent shall within thirty (30) days after the date of service of this order, amend its charter, by-laws, rules and regulations by eliminating therefrom any provision which is contrary to or inconsistent with any provision of this order, and that respondent shall thereafter require as a condition of membership that all present and future members of respondent act in accordance with the provisions of this order.

It is further ordered, That respondent shall keep full and complete records relating to the following and shall retain the same for 3 years:

(a) standards for admission to and retention of membership in the respondent;

(b) all denials of membership in the respondent;

(c) all expulsions or withdrawals from, or non-renewals of membership in the respondent;

(d) all correspondence and minutes, formal or informal, kept by or on behalf of the respondent and its committees.

It is further ordered, That respondent trade association notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

It is further ordered, That the respondent herein shall within sixty

(60) days after service upon it of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it complied with this order including copies of all affidavits required by this order to be obtained by the respondent.

IN THE MATTER OF

CHILDREN'S ADVERTISING

TRR. 215-60. Interlocutory Order, Jan. 9, 1979

ORDER DENYING JOINT APPEAL

By letter of December 28, 1978, and motion of December 20, 1978, the Chocolate Manufacturers Association, Kellogg Company, Association of National Advertisers, and Toy Manufacturers Association have urged the Commission to review the Presiding Officer's Orders No. 39 and 41.

The Presiding Officer has declined to certify this matter to the Commission for review because it does not involve a "controlling question of law or policy as to which there is substantial ground for difference of opinion, nor has there been a showing that an immediate review of this ruling will materially advance the ultimate termination of this proceeding or that subsequent review will be an inadequate remedy." (Order No. 39, pp. 9-10)

The Commission's Rules of Practice provide that the Commission will not entertain applications for review of an uncertified Order of the Presiding Officer prior to its final review of the record, 16 C.F.R. 1.13(c)(i), except in the limited circumstances described in 16 C.F.R. 1.13(c)(2)(ii). This matter does not involve any of those circumstances.

It is ordered, That petitioners' "Joint Appeal" and letter seeking review of Presiding Officer's Orders No. 39, and 41 be denied.

Chairman Pertschuk and Commissioner Pitofsky did not participate.

IN THE MATTER OF

ART INSTRUCTION SCHOOLS, INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2949. Complaint, Jan. 10, 1979 — Decision, Jan. 10, 1979

This consent order, among other things, requires a Minneapolis, Minn. firm, engaged in the formulation and sale of home study courses, its subsidiary, Art Instruction Schools, Inc. (AIS), and its New York City advertising agency to cease misrepresenting the need or demand for AIS graduates; and the employment opportunities, potential earnings, and job placement assistance available to graduates. The order further prohibits misrepresentations relating to student selectivity; quality of art courses; additional costs; and penalties incurred by non-completing enrollees. The order also requires that prospective students be provided with prescribed information relating to the job success of former enrollees, and informed of their cancellation rights. Additionally, the companies must make proper restitution to former students; maintain particular records; and institute a surveillance program designed to insure compliance with the terms of the order.

Appearances

For the commission: *Alice S. Perlin.*

For the respondents: *Micheal F. Sullivan, Gray, Plant, Mooty & Anderson,* Minneapolis, Minn.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Bureau of Engraving, Inc., a corporation, Art Instruction Schools, Inc., a corporation, and Bozell & Jacobs, Inc., a corporation, hereinafter sometimes referred to as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Bureau of Engraving, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Minnesota with its principal office and place of business located at 500 South Fourth St., Minneapolis, Minnesota.

Respondent Art Instruction Schools, Inc., (hereinafter sometimes referred to as "AIS"), is a corporation organized, existing and doing business under and by virtue of the laws of the State of Minnesota, with its principal office and place of business located at 500 South

Fourth St., Minneapolis, Minnesota. It is a wholly-owned subsidiary of respondent Bureau of Engraving, Inc.

Respondent Bozell & Jacobs, Inc. is a corporation organized and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business at One Dag Hammarskjold Plaza, New York, New York.

PAR. 2. Respondent Art Instruction Schools, Inc. is now and for some time last past has been engaged in the formulation, development, promotion, offering for sale, sale, and distribution of courses of instruction to the public. Said respondent, through its own salesmen and sales representatives, have induced members of the general public to enroll in its courses of instruction.

Said respondent places into operation and implements a sales program whereby members of the general public, by means of advertisements placed in broadcast and printed media of general circulation, and by means of brochures, pamphlets and other promotional literature disseminated through the United States mail or by other means, and through the use of salesmen and sales personnel, and by means of statements, representations, acts and practices as hereinafter set forth are induced to sign contracts or enrollment agreements for a course of home study instruction for a stated cost.

Respondent Bureau of Engraving, Inc. indirectly benefits from sales made by Art Instruction Schools, Inc. and derives substantial income therefrom. Bureau of Engraving, Inc. further knew or had reason to know of the activities engaged in by AIS and its employees.

PAR. 3. Respondent Bozell & Jacobs, Inc. has been and is now the advertising agency for Art Instruction Schools Inc., and has prepared and placed for publication and broadcast, and caused the dissemination of, advertising material, including but not limited to advertising as hereinafter set forth to promote the sale of respondent AIS' courses of instruction.

PAR. 4. In the course and conduct of their business as aforesaid, respondents have disseminated and caused the dissemination of certain advertisements concerning their courses of instruction by various means in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, including, but not limited to, advertisements inserted in newspapers and magazines of interstate circulation, and by means of commercial announcements over television transmitted across state lines, and by means of brochures, pamphlets and other promotional materials disseminated through the United States mail, for the purpose of obtaining leads or prospects for the sale of such courses of instruction, and for the purpose of inducing the purchase of such courses of instruction. Each of said respondents' volume of business in commerce is substantial.

Respondent Art Instruction Schools, Inc., from its principal place of business located in Minnesota, utilizes the services of sales representatives and causes said sales representatives to visit prospective purchasers located in various other States of the United States who respond to respondents' advertisements and commercial announcements for the purpose of inducing the purchase of such courses of instruction by such prospective purchasers.

Respondents transmit and receive and cause to be transmitted and received, in the course of advertising, offering for sale, sale and distribution of such courses of instruction, advertising and promotional materials, sales contracts, invoices, billing statements, checks, monies and other business papers and documents, to and from their principal places of business operated by said respondents located as aforesaid and to prospective purchasers and purchasers thereof located in various other States of the United States. Respondents maintain, and at all times mentioned herein have maintained, a substantial course of trade in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 5. In the course and conduct of Art Instruction Schools, Inc.'s aforesaid business for the purpose of obtaining leads or prospects for the sale of such courses of instruction, and for the purpose of inducing members of the general public to purchase such courses of instruction, respondents Art Instruction Schools, Inc. and Bozell & Jacobs, Inc. have made numerous statements and representations in newspaper advertisements, television commercials, brochures, and other printed materials and sales aids and through oral sales presentations made by respondent AIS' salespersons and other representatives, with respect to employment opportunities, salaries available, placement assistance and other benefits available to students who complete respondent AIS' courses of instruction. The following are typical and illustrative of the aforesaid statements and representations, but not all inclusive thereof:

A. Magazine and newspaper advertisements:

YOU BE THE JUDGE

Have you ever thought an art career is the career for me? Do you sometimes doodle or draw? If so, you may have the talent for a profitable and exciting career in art . . . make up your mind whether or not you want to learn more about the great opportunities in the art field, . . . We'll send you a copy of your free Art Talent Test. It's colorful, interesting and it may lead to a rewarding and challenging art career.

B. Television advertisements:

. . . In a moment I'll tell you how to find out, *Free,* if you have the basic talent needed to help you become a successful working artist. Here are just a few fields where good artists are usually needed. Advertising, Calendar Art, Fashion Illustration, Greeting Card Design, Magazine Illustration, Motion Picture Art, Newspaper Cartooning, Television Art . . . New talent is welcome in the art field. . . .

C. Video Tape Sales Aid:

. . . We've been training commercial artists since 1914 . . . we already know some important things about *you.* We've seen your art work. We know of your interest in art. In fact, *if we didn't think you have something special we wouldn't be here.* . . .

D. Statements from Letters, Pamphlets and Brochures:

. . . This may be your big opportunity to take that first step toward being a successful advertising artist, illustrator, painter or cartoonist. The enclosed brochures tell of the success of just two of our well known former students — Charles Schultz, creater of the famous "Peanuts" cartoon strip, and Les Kouba, successful wildlife illustrator.

Our artist appraiser feels that you have artistic ability which should be trained . . . we would not encourage any person to invest in our practical art training unless we were convinced that he had the desire and determination to succeed in this expanding and interesting profession. . . .

E. Oral Statements by Sales Representatives:

AIS students encounter little difficulty obtaining employment as artists in the field of commercial art.

* * * * * * *

AIS graduates are entitled to life time job placement in the field of commercial art.

* * * * * * *

AIS graduates earn salaries between $15,000 - $25,000 annually.

PAR. 6. By and through the use of the aforementioned statements and representations, and others of similar import and meaning, but not expressly set out herein, respondents represent or have represented directly or by implication, that:

1) Respondent AIS provides a placement service which will secure jobs for its graduates who want to work in the field of art or related areas.

2) The courses of instruction offered by respondent AIS are equivalent to studio art courses offered by accredited colleges or universities.

3) The total enrollment fee as listed on respondent AIS' Enroll-

ment Agreement includes the cost of all books, supplies and materials that students will have to bear.

4) Students of AIS may withdraw from or cancel courses of instruction at any time without paying additional monies or charges.

5) Prospective students of AIS must enroll at the time of the sales representative's visit or they will lose their opportunity for acceptance into the courses of instruction.

PAR. 7. In truth and fact:

1) No placement service is provided by respondent AIS for its graduates who want to secure jobs in the field of art or related areas.

2) The courses of instruction offered by respondent AIS are not substantially equivalent to studio art courses offered by accredited colleges and universities.

3) The total enrollment fee as listed on respondent AIS' Enrollment Agreement does not include the total cost of all books, supplies and materials that students will have to bear.

4) Students of AIS may not withdraw from or cancel courses of instruction at any time without paying additional monies or charges, but are bound to the terms of the Withdrawal provisions of the Enrollment Agreement.

5) Prospective students of AIS will not lose their opportunity for acceptance into the courses of instruction if they do not enroll at the time of the sales representative's visit, and are free to enroll at any future date.

Therefore, the statements and representations in Paragraphs Five and Six hereof were and are, false, misleading, unfair or deceptive acts or practices.

PAR 8. In the further course and conduct of its business of selling or inducing the sale of said courses of instruction, as aforesaid, and by means of the statements and representations set out in Paragraphs Five and Six hereof, respondents made the following additional statements and representations, directly or indirectly, to prospective students in said courses of instruction:

1) Respondent AIS is very selective and will only accept applications for its courses of instruction that have artistic talent and ability.

2) Respondent AIS had a reasonable basis from which to conclude that there is now or will be a significant or substantial need or demand in the field of art for persons who complete its courses of instruction.

3) AIS graduates who want to work will experience little or no

difficulty in securing employment in positions in the field of art after graduating from said courses.

4) AIS graduates will be qualified thereby for employment in the field of art without further training or experience.

5) Respondent AIS had a reasonable basis from which to conclude that its graduates earn $15,000 to $25,000 annually or any other stated amount in the field of art.

PAR. 9. In truth and in fact:

1) Respondent AIS is not selective in accepting applicants for their courses of instruction, imposing few qualifications on prospective enrollees and accepts most persons for enrollment in such courses who are willing to execute a contract and pay the required tuition for the course of training.

2) Respondent AIS had no reasonable basis from which to conclude that there is now or will be a significant or substantial need or demand in the field of art for persons who complete its courses of instruction.

3) AIS graduates who want to work have in many instances experienced substantial difficulty in securing employment in positions in the field of art.

4) AIS graduates are not qualified thereby for employment in the field of art without further training or experience.

5) Respondent AIS had no reasonable basis from which to conclude that its graduates have earned or can earn $15,000 to $25,000 annually or any other stated amount in the field of art.

Therefore, the statements and representations set forth in Paragraphs Five and Eight hereof were and are, false, misleading, unfair, or deceptive acts or practices.

PAR. 10. Through the use of the aforesaid advertisements, television commercials, brochures, pamphlets, oral representations and otherwise, respondent Art Instruction Schools, Inc. has represented directly or by implication, that there is or will be a significant or substantial need or demand for all or most graduates of respondent AIS in positions for which they are trained; and that graduates of respondent AIS are placed in jobs and earn $15,000 to $25,000 annually or other stated amounts in the field of art. Respondent had at the time of said representations no reasonable basis adequate to support the representations. Therefore, the aforesaid acts and practices were and are, unfair acts or practices.

PAR. 11. In the further course and conduct of its business and in the furtherance of its purpose of inducing students to pay delinquent accounts, respondent AIS has sent to its students collection letters stating that failure to pay the amount claimed as owing within a stated period of time will result in immediate legal action. To the contrary, no lawsuit has ever been filed to collect a delinquent account on a student's failure to pay upon receipt of such a letter. Therefore, said statements and representations made by respondents were and are unfair, false, misleading or deceptive acts or practices.

PAR. 12. In the course and conduct of its aforesaid business, and at all times mentioned herein, respondent Art Instruction Schools, Inc. has offered, and is now offering for sale courses of instruction purporting to prepare purchasers thereof for positions in the field of art without disclosing in advertising or through their sales representatives: (1) the recent percentage of persons who have completed the courses of instruction who were able to obtain the employment for which they were trained; (2) the salary any such persons can earn; and (3) the percentage of recent enrollees of each course offered that have failed to complete their course of instruction. Knowledge of such facts by prospective purchasers of courses of instruction of respondents AIS would indicate the possibility of securing future employment upon completion of the courses, and the nature of such employment. Thus, said respondent has failed to disclose a material fact which, if known to certain consumers, would be likely to affect their consideration of whether or not to purchase such courses of instruction. Therefore, the aforesaid acts and practices were and are, false, misleading, deceptive or unfair acts or practices.

PAR. 13. In the further course and conduct of its business and in the furtherance of its purpose of enrolling students in its courses of instruction, respondents have advertised free Art Talent Tests and sponsored periodic drawing contests without disclosing that their primary purpose was to obtain leads to prospective students who could be visited by respondent AIS' sales representatives and induced to enroll in an $845 home study art course. Therefore, the aforesaid acts and practices are deceptive or unfair.

PAR. 14. By and through the use of the aforesaid acts and practices, respondents place in the hands of others the means and instrumentalities by and through which they may mislead and deceive the public in the manner and as to the things hereinabove alleged.

PAR. 15. In the course and conduct of their business, and at all times mentioned herein, respondents Bureau of Engraving, Inc. and Art Instruction Schools, Inc. have been and are now in substantial competition, in commerce, with corporations, firms, and individuals engaged in the sale of courses of instruction covering the same or similar subjects.

In the course and conduct of its business, and at all times mentioned herein, respondent Bozell & Jacobs, Inc. has been and is now in substantial competition in commerce, with corporations, firms and individuals engaged in the advertising of home study schools' courses of instruction covering the same or similar subjects.

PAR. 16. The use by respondents of the aforesaid false, misleading, unfair or deceptive statements, representations, acts and practices and their failure to disclose material facts as aforesaid has had, and now has, the tendency and capacity to mislead and deceive a substantial portion of the purchasing public into the erroneous and mistaken belief that said statements and representations were, and are, true and complete, and induce a substantial number thereof to purchase courses of instruction from respondent AIS by reason of said erroneous and mistaken belief.

PAR. 17. The aforesaid acts and practices of respondents Bureau of Engraving, Inc., Art Instruction Schools, Inc., and Bozell & Jacobs, Inc., as herein alleged, were and are all to the prejudice and injury of the public and said respondents' competitors and constituted, and now constitute, unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of the draft of complaint which the Chicago Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having hereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, that the complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Bureau of Engraving, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Minnesota with its principal office and place of business located at 500 South Fourth St., Minneapolis, Minnesota.

Respondent Art Instruction Schools, Inc., (hereinafter sometimes referred to as AIS), is a corporation organized, existing and doing business under and by virtue of the laws of the State of Minnesota, with its principal office and place of business located at 500 South Fourth St., Minneapolis, Minnesota. It is a wholly-owned subsidiary of respondent Bureau of Engraving, Inc.

Respondent Bozell & Jacobs, Inc. is a corporation organized and doing business under and by virtue of the State of Delaware, with its principal office and place of business at One Dag Hammarskjold Plaza, New York, New York.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

Order

I

It is ordered, That respondents, Bureau of Engraving, Inc., and Art Instruction Schools, Inc., hereinafter sometimes referred to as "AIS", their successors and assigns, and their officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division or other device, in connection with the advertising, offering for sale, sale or distribution of courses of study, training or instruction in the field of art or in any other subject, trade or vocation in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. Representing, orally, visually, in writing or in any other manner, directly or by implication that:

(A) A placement service is provided which will or may secure a position in the field of art for graduates of respondent AIS courses of instruction;

(B) Respondent AIS courses of instruction are equivalent to college level art courses in specialized studio art subjects offered by accredited colleges or universities;

(C) Respondent AIS students are not contractually bound, or by the nature of the course not required, to bear any expenses or costs in addition to those set out in the enrollment agreement or is otherwise stated prior to enrollment;

(D) Respondent AIS students will be entitled to withdraw from the courses of instruction without having to adhere to the withdrawal payment schedule contained in the contract or without paying any undisclosed charges in addition thereto;

(E) Respondent AIS prospective students must enroll at the time of the sales representative's visit, or that they will have no other opportunity to enroll.

2. Misrepresenting orally, visually, in writing or in any other manner, directly or by implication:

(A) That enrollees in respondent AIS courses of art instruction will be required to qualify under highly selective procedures, or that enrollment is limited or that other significant limiting criteria are applicable;

(B) (i) that there is a great need or great demand or need or demand of any size for persons completing any of AIS courses of instruction;

(ii) that AIS graduates will experience little or no difficulty in securing employment in positions for which they were trained; or

(iii) the employment or earning prospects of AIS graduates in positions for which they have been trained;

(C) That graduates of respondent AIS will be qualified thereby for full or part time positions in the field of art utilizing their artistic skills without further training or experience;

(D) That respondents will initiate legal action against delinquent students.

3. Failing to furnish written notice to the person to be contacted, prior to initial contact by a sales representative, that a sales representative of respondent AIS may contact persons who respond to the free Art Talent Tests or drawing contests.

4. Failing orally to direct each prospective enrollee's attention, at the time he or she signs a contract or agreement for the sale of any course of instruction to the provisions of the contract or agreement which set forth his or her contractual right to cancel.

5. Making any representations of any kind whatsoever, which are not already proscribed by other provisions of this order, in connection with the advertising, promoting, offering for sale, sale or distribution of courses of study, training or instruction in the field of art, or any other course offered to the public in any field in

commerce, for which representation respondent AIS has no reasonable basis prior to the making or dissemination thereof.

6. *It is further ordered*, That respondent Bozell & Jacobs, Inc., a corporation, its successors and assigns and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division, franchise or other device on behalf of AIS in connection with the advertising, promoting, offering for sale, sale or distribution of courses of study, training or instruction in the field of art or any other subject, trade or vocation or of any other product or service in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

(A) Misrepresenting orally, visually, in writing or in any other manner, directly or by implication, that;

(i) enrollees in respondent AIS courses of art instruction will be required to qualify under highly selective procedures, or that enrollment is limited or that other significant limiting criteria are applicable;

(ii) graduates of respondent AIS will be qualified thereby for full or part time positions in the field of art utilizing their artistic skills without further training or experience;

(iii) there is a great need or great demand or need or demand of any size for persons completing any of AIS courses of instruction;

(iv) AIS graduates will experience little or no difficulty in securing employment in positions for which they are trained; or

(B) Making any representations of any kind whatsoever, which are not already proscribed by other provisions of this order, in connection with the advertising, promoting, or offering for sale of respondent AIS courses of study, training or instruction in the field of art or any other course offered to the public in any field in commerce, for which respondent has no reasonable basis prior to the making or dissemination thereof.

(C) Failing to deliver a copy of this order to cease and desist to all present and future personnel of respondent Bozell & Jacobs engaged in preparing, creating or reviewing advertisements on behalf of any client engaged in the home study and correspondence school business, and secure from each such person a signed statement acknowledging receipt of said order.

II

1. *It is further ordered,* That respondents Bureau of Engraving, Inc. and Art Instruction Schools, Inc.:

(A) Deliver, or cause to be delivered, a copy of this decision and order to licensees, employees, sales representatives, agents, solicitors, independent contractors, or to any other person, who promotes, offers for sale, sells or distributes any course of instruction included within the scope of this order.

(B) Provide each person or entity so described in Paragraph 1(A) of Part II of this order with a form returnable to the respondents clearly stating his or her intention to be bound by and to conform his or her business practices to the requirements of this order, retain said statement during the period said person or entity is so engaged, and make said statement available to the Commission's staff for inspection and copying upon request.

(C) Inform each person so described in Paragraph 1(A) above that the respondents will not use or engage or will terminate the use or engagement of any such party, unless such party agrees to and does file notice with the respondents that he or she will be bound by the provisions contained in this order.

(D) If such party as described in Paragraph 1(A) above will not agree to file the notice set forth in Paragraph 1(B) above with the respondents and be bound by the provisions of this order, the respondents shall not use or engage or continue to use the engagement of such party to promote, offer for sale, sell or distribute any course of instruction included within the scope of this order.

(E) Inform the persons or entities in Paragraph 1(A) above that the respondents are obligated by this order to discontinue dealing with or to terminate the use or engagement of persons or entities who continue on their own the deceptive acts or practices prohibited by this order.

(F) Institute a program of continuing affirmative compliance review reasonably designed to establish whether the business practices of each said person or entity described in Paragraph 1(A) above conform to the requirements of this order.

(G) Discontinue dealing with or terminate the use or engagement of any person described in Paragraph 1(A) above as revealed by the aforesaid compliance review programs, who continues on his or her own any act or practice prohibited by this order.

III

1. *It is further ordered,* That for the purposes of Part III the following definitions shall apply:

(A) The term "Relevant Period" shall mean the four year period commencing January 1, 1972 and continuing through December 31, 1975 in respect to the "Graduate List," and commencing March 1,

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1973 and continuing through October 1, 1976 in respect to "Non-Completing Students."

(B) The term "Graduate List" shall mean the list of names and addresses of students, who reside in the United States, of any individual course of instruction offered for sale by respondent AIS in the field of art, who within the "Relevant Period" have completed the number of lessons required by respondent AIS for completion of individual courses, irrespective of the date of such students' enrollment in or commencement of such course, and irrespective of the amount of tuition paid by such students.

(C) The term "Non-Completing Student" shall mean students, who reside in the United States (other than those whose names appear on the "Graduate List"), who have enrolled in a course of instruction of respondent AIS in the field of art on or after March 1, 1973, (1), who, after completing one-half (1/2) or more of respondent AIS program of art instruction, have during the "Relevant Period" affirmatively notified respondent AIS in writing of his or her intention to terminate or not to complete the program of instruction or have been terminated as a student by respondent AIS, or (2) who, after completing two-thirds (2/3rds) or more of respondent AIS program of art instruction, have not submitted a lesson during any continuous twelve (12) month period during the "Relevant Period" without the student having requested and been granted an extension of time in which to complete the program. For purposes of this order, "two-thirds" of the AIS program shall mean completion of 18 lessons in the 27 lesson program or 10 lessons in the 14 lesson program, as the case may be.

(D) The term "Non-Completion List" shall include each "Non-Completing Student" of any individual course of instruction offered for sale by AIS in the field of art.

2. *It is further ordered,* That respondents Bureau of Engraving, Inc., and Art Instruction Schools, Inc., shall within sixty (60) days from the date of acceptance of this order by the Federal Trade Commission, compile two (2) separate lists. The first list shall be entitled "Graduate List" and shall contain the last known names and addresses of all students who qualify for inclusion therein pursuant to the criteria set forth in Part III, Paragraph 1(B), and shall also contain the names and addresses of such students' nearest relative(s) whose addresses appear on any document in respondents' files relating to said students. The second list shall be entitled "Non-Completion List" and shall contain the last known names and addresses of all "Non-Completing Students" who qualify for inclusion therein pursuant to the criteria set forth in Part III, Paragraph

1(C) and shall also contain the names and addresses of such students' nearest relative(s) whose addresses appear on any document in respondents' files relating to said student. Respondent shall prepare the "Graduate List" and "Non-Completion List" from respondents' records in their respective possession, custody or control. The "Graduate List" and "Non-Completion List" shall be supplemented by a list of persons in the same respective categories compiled by the Federal Trade Commission and transmitted to said respondents within one hundred five (105) days from the date of acceptance of this order by the Federal Trade Commission.

3. *It is further ordered,* That respondents Bureau of Engraving, Inc., and Art Instruction Schools, Inc., shall jointly, within sixty (60) days from the effective date of this order, retain an independent contractor acceptable to the Commission, and give to said independent contractor, within one hundred ten (110) days from the date of acceptance of this order by the Federal Trade Commission, the "Graduate List," "Non-Completion List" and the list of persons in the same respective categories provided to respondents by the Federal Trade Commission. Said independent contractor shall review the lists, strike out any duplication of names and addresses of students set forth in such lists, and determine the due qualification of each student listed to be included in such lists under the criteria hereinabove referred to. Said independent contractor shall be granted access to respondents' records in order to prepare a final "Graduate List" and a final "Non-Completion List." Students whose names appear on the final lists in each category as compiled by the independent contractor are to receive one or more of the Appendices A, B, C, D and E in accordance with the following provisions of Part III of this order. No student shall be included or retained on any final list compiled by the independent contractor who, in the good faith judgment of the independent contractor, on the basis of respondents' records, is manifestly not entitled to participate in the restitution contemplated by the order by reason of not meeting the substantive criteria therefore established in Part III, Paragraphs 6 and 9 below.

Graduate List

4. (A) *It is further ordered,* That said independent contractor shall make an inquiry in writing on the one hundred thirtieth (130) day after the effective date of this order to all students whose names and addresses appear on the "Graduate List," in the language, manner and form shown in Appendices A and D, by first class mail and with a self-addressed postage prepaid return envelope. Said inquiry shall be known as the "first mailing." With respect to all

students whose "first mailing" is returned unopened on or prior to the two hundredth (200) day after the effective date of this order, said independent contractor shall within three (3) days after such "first mailing" is returned unopened attempt by reasonable mailed inquiry to establish contact with such students by requesting by mail new addresses from the students' nearest relative(s) whose addresses appear on any document supplied to the independent contractor through which a student may be located. Said independent contractor upon securing a new address from the aforementioned source shall initiate the "first mailing" procedure to the new address of the student.

(B) Said independent contractor shall make a second inquiry in writing on the one hundred seventieth (170) day after the effective date of this order to all students whose names and addresses appear on the "Graduate List" and have not responded to the "first mailing" of the independent contractor by such date. The second inquiry in writing by first class mail and with a self-addressed postage prepaid return envelope shall be known as the "second mailing" and be in the language, manner and form shown in Appendix B.

(C) Said independent contractor shall make a third inquiry in writing on the two hundredth (200) day after the effective date of the order to all students whose names and addresses appear on the final "Graduate List" and have not responded to the "first mailing" or "second mailing" of the independent contractor by such date. The third inquiry in writing by first class mail and with a self-addressed postage prepaid return envelope shall be known as the "third mailing" and shall be in the language, manner and form shown in Appendix C.

5. *It is further ordered,* That:

(A) At the expiration of forty-five (45) days after the independent contractor mails the "third mailing," and in any event two hundred forty-five (245) days after the effective date of this order, said contractor shall transmit to respondents all Appendix D responses it has received by such date; and

(B) Respondents' obligation to make restitution shall extend to those persons whose names appeared on the final "Graduate List" compiled by the independent contractor and whose Appendix D responses have been received by the independent contractor on or before the expiration of said forty-five (45) day period and whose eligibility is certified by the independent contractor pursuant to Paragraph 5(C) of Part III of this order below; and

(C) The independent contractor shall certify to respondents the identity of all students eligible to receive restitution on the basis of their Appendix D responses. The independent contractor shall be the final judge in good faith of such eligibility based upon the criteria set forth in Part III, Paragraphs 1, 5 and 6 of this order.

6. *It is further ordered,* That on the thirtieth (30) day following the close of the forty-five (45) day period described in Part III, Paragraph 5(A) of this order, and in any event two hundred seventy-five (275) days after the effective date of this order, respondents shall refund to those students of AIS courses identified by the independent contractor as eligible therefore an amount equal to twenty-five percent (25%) of an amount equal to the gross tuition paid by each student to respondent AIS for any such course, less any previous refunds. With respect to each such student on the "Graduate List" deemed eligible to receive a refund of tuition, respondents shall forward to each such person together with the refund check a notice in the following language:

> This refund check is tendered in satisfaction of all claims by you against Art Instruction Schools, Inc., Bureau of Engraving, Inc., and the officers, directors, employees and agents of either of them. Upon acceptance of the refund check each of the foregoing shall be released from all such claims by you arising out of the payment of tuition for any Art Instruction Schools, Inc., course of instruction, and you shall be released from all claims by Art Instruction Schools, Inc., or Bureau of Engraving, Inc., against you.

In addition to the refund of the percentage of gross tuition specified herein, respondents shall also refund to each student on the "Graduate List" who qualifies hereunder for a refund, the amount of tuition payments made by said student to respondents between the effective date of this order and a date not more than ten (10) days prior to the date the refund check is due to be mailed to said student under the foregoing schedule. In order for any student on the "Graduate List" to be eligible to receive a refund of tuition, such student must satisfy the following criteria, in addition to the procedural requirements of Part III, Paragraph 4 of this order:

(A) The student enrolled in an AIS course of instruction for the purpose of obtaining employment in the field of art utilizing his or her artistic skills or to improve his or her level of employment as an artist by virtue of training received from such course of instruction; and

(B) (i) sought employment in the field of art utilizing his or her artistic skills, or

(ii) for reasons relating to the lack of sufficiency or quality of AIS training, or lack of relevant employment opportunity, elected not to seek such employment; and

(C) Did not obtain employment in the field of art or did not improve his or her level of employment, notwithstanding the training received from AIS.

Non-Completion List

7. (A) *It is further ordered,* That the independent contractor shall make an inquiry in writing on the one hundred thirtieth (130) day after the effective date of this order to all students whose names and addresses appear on the final "Non-Completion List" compiled by the independent contractor, in the language, manner and form shown in Appendices A and E by first class mail and with a self-addressed postage prepaid return envelope. Said inquiry shall be known as the "first mailing." With respect to all students whose "first mailing" is returned unopened on or prior to the two hundredth (200) day after the effective date of this order said independent contractor shall, within three (3) days after such "first mailing" is returned unopened, attempt by reasonable mailed inquiry to establish contact with such students by requesting by mail new addresses from the students' nearest relative(s) whose addresses appear on any document supplied to the independent contractor through which a student may be located. Said independent contractor upon securing a new address from the aforementioned source shall initiate the "first mailing" procedure to the new address of the student.

(B) Said independent contractor shall make a second inquiry in writing on the one hundred seventieth (170) day after the effective date of this order to all students whose names and addresses appear on the final "Non-Completion List" and have not responded to the "first mailing" of the independent contractor by such date. The second inquiry in writing by first class mail and with a self-addressed postage prepaid return envelope shall be known as the "second mailing" and be in the language, manner and form shown in Appendix B.

(C) Said independent contractor shall make a third inquiry in writing on the two hundredth (200) day after the effective date of this order to all students whose names and addresses appear on the final "Non-Completion List" and have not responded to the "first mailing" or "second mailing" of the independent contractor by such date. The third inquiry in writing by first class mail and with a self-addressed postage prepaid return envelope shall be known as the "third mailing" and be in the language, manner and form shown in Appendix C.

8. *It is further ordered,* That:

(A) At the expiration of forty-five (45) days after the independent contractor mails the "third mailing," and in any event two hundred forty-five (245) days after the effective date of this order, said contractor shall transmit to respondents all Appendix E responses it has received by such date; and

(B) Respondents' obligation to make restitution shall extend to those persons whose names appeared on the final "Non-Completion List" compiled by the independent contractor and whose Appendix E responses have been received by the independent contractor on or before the expiration of said forty-five (45) day period and whose eligibility is certified by the independent contractor pursuant to Paragraph 8(C) of Part III of this order below; and

(C) The independent contractor shall certify to respondents the identity of all students eligible to receive restitution on the basis of their Appendix E responses. The independent contractor shall be the final judge in good faith of such eligibility based upon the criteria set forth in Part III, Paragraphs 1, 8 and 9 of this order.

9. *It is further ordered,* That on the thirtieth (30) day following the close of the forty-five (45) day period described in Part III, Paragraph 8(A) of this order, and in any event two hundred seventy-five (275) days after the effective date of this order, respondents shall refund to those students of AIS courses identified by the independent contractor as eligible therefore an amount equal to twenty percent (20%) of an amount equal to the gross tuition paid by each student to respondent AIS for any such course, less any previous refunds. With respect to each such student on the "Non-Completion" deemed eligible to receive a refund of tuition, respondents shall forward to each such person together with the refund check a notice in the following language:

> This refund check is tendered in satisfaction of all claims by you against Art Instruction Schools, Inc., Bureau of Engraving, Inc., and the officers, directors, employees and agents of either of them. Upon acceptance of the refund check each of the foregoing shall be released from all such claims by you arising out of the payment of tuition for any Art Instruction Schools, Inc., course of instruction, and you shall be released from all claims by Art Instruction Schools, Inc., or Bureau of Engraving, Inc., against you.

In order for any student on the final "Non-Completion List" to be eligible to receive a refund of tuition such student must satisfy the following criteria, in addition to the procedural requirements of Part III, Paragraph 8 of this order:

(A) The student enrolled in an AIS course of instruction for the purpose of obtaining, during the conduct of the course of instruction, employment in the field of art utilizing his or her artistic skills, or during the conduct of the course to improve his or her level of employment as an artist by virtue of training received from such course of instruction; and

(B) (i) sought employment in the field of art utilizing his or her artistic skills, or (ii) for reasons relating to the lack of sufficiency or quality of AIS training, or lack of relevant employment opportunity, elected not to seek such employment; and

(C) Did not during the conduct of the course or thereafter obtain employment in the field of art or did not during the conduct of the course or thereafter improve his or her level of employment, notwithstanding the training received from AIS.

10. *It is further ordered,* That notwithstanding any provision of Part III, Paragraphs 1 through 9 to the contrary, any amount payable as restitution thereunder shall be remitted to the person appearing on the records of respondents as the person who actually paid the tuition being refunded if such person is different from the qualifying student who enrolled in such course(s).

IV

It is further ordered, That respondents Bureau of Engraving, Inc., and Art Instruction Schools, Inc., maintain in their respective student files all documents and writings relating to inquiries or complaints from any source relating to acts or practices prohibited by this order for a period of two (2) years after the effective date of this order, and that such files be made available for examination by a duly authorized agent of the Federal Trade Commission during the regular hours of the respondents' business for inspection and copying.

V

It is further ordered, That respondents Bureau of Engraving, Inc. and Art Instruction Schools, Inc. shall forthwith distribute a copy of this order to each of their operating divisions.

VI

It is further ordered, That respondents Bureau of Engraving, Inc., Art Instruction Schools, Inc. and Bozell & Jacobs, Inc. shall notify the Commission at least thirty (30) days prior to any proposed change in respondents such as dissolution, assignment or sale resulting in the emergence of a successor corporation, or any other change in respondents which may affect compliance obligations arising out of this order.

VII

It is further ordered, That in the event the Federal Trade Commission promulgates a final Trade Regulation Rule on Advertising, Disclosure, Cooling-Off and Refund Requirements Concerning Proprietary, Vocational and Home-Study Schools, then such trade regulation rule shall completely supercede and replace the provisions of this order set forth in Part I, Paragraphs 2 through 4 *provided,* that if no provision of the trade regulation rule relates in whole or in part to any matter covered by provisions of one of the aforesaid paragraphs of this order, the said provisions of said paragraph shall remain in full force and effect.

VIII

It is further ordered, That no provision of this order shall be construed in any way to annul, invalidate, repeal, terminate, modify or exempt respondents from complying with agreements, orders or directives of any kind obtained by any other agency or act as a defense to actions instituted by municipal or state regulatory agencies. No provision of this order shall be construed to imply that any past or future conduct of respondents complies with the rules and regulations of, or the statutes administered by the Federal Trade Commission.

IX

It is further ordered, That each respondent herein named shall, within sixty (60) days after service upon it of this order, file with the Commission a report in writing setting forth the manner and form in which each has complied with this order, and respondents Bureau of Engraving, Inc., and Art Instruction Schools, Inc., shall, within two hundred seventy (270) days after the independent contractor first mails the "first mailings" referred to in Part III above, file with the Commission a report in writing setting forth the manner and form in which they have complied with Part III of this order.

APPENDIX A

Important Notice

(Name of Addressee)
(Address of Addressee)

Subject: Your enrollment in Art Instruction Schools, Inc.

Dear ________________:

We would like you to help us by filling out the enclosed short questionnaire.

The Federal Trade Commission has directed us to get certain facts and information from you concerning your association and relationship with our school. We have asked (name of independent contractor) to get this information from the questionnaire. Art Instruction Schools, Inc. will use the gathered information to meet important legal obligations to former students such as yourself.

It is very important that you promptly provide the information requested. Please fill out the questionnaire and return it in the enclosed return envelope. If you have any questions about this letter or the questionnaire, please contact (name of person, independent contractor, address, and telephone number).

Sincerely yours,

Roy O. Stuart
President
Art Instruction Schools, Inc.

APPENDIX B

Important Notice

(Name of Addressee)
(Address of Addressee)

Subject: Your enrollment in Art Instruction Schools, Inc.

Dear ________________:

Approximately one month ago we asked you to fill out a questionnaire about your association and relationship with Art Instruction Schools, Inc. We have not received your response.

The information requested is *very* important in order to fulfill important legal obligations to our former students such as yourself. Please help us by filling out the questionnaire and returning it in the enclosed envelope.

If you have any questions regarding this letter please contact (name of person, independent contractor, address, and telephone number).

Sincerely yours,

Roy O. Stuart
President
Art Instruction Schools, Inc.

APPENDIX C

Important Notice

(Name of Addressee)
(Address of Addressee)

Subject: Your enrollment in Art Instruction Schools, Inc.

Dear ________________:

Twice during the past two months we asked you to fill out an important questionnaire regarding your association and relationship with Art Instruction Schools, Inc. We have not received your response.

The Federal Trade Commission has directed the School to compile this information to meet important legal obligations to former students such as yourself. The only method to determine the existence and scope of such legal obligations to former students is by you filling out the questionnaire. Please do so as soon as possible and return it in the enclosed envelope. If you have any questions please contact (name of person, independent contractor, address, and telephone number).

Sincerely yours,

Roy O. Stuart
President
Art Instruction Schools, Inc.

APPENDIX D

Subject: Your enrollment in Art Instruction Schools, Inc. ("AIS") Minneapolis, Minnesota.

1. Is your current address correctly shown on the envelope?
   Yes ( ) No ( ) If not, what is your address?
2. (a) About when did you sign up for the AIS course?

   ____
   Month and Year

   (b) About when did you make your first payment to AIS?

   ____
   Month and Year
3. What was the name of the course?
4. (a) Did you finish the course in which you enrolled?
   Yes ( ) No ( )

   (b) If you finished the course, about when did you do so?

   ____
   Month and Year
5. What was the total amount of money you paid for your course?
   (Total amount paid: $______________)
6. People take a correspondence course for various reasons. Which *one* of the reasons listed below best fits your own reason for taking the course? (Read all reasons first before you check *ONE*.)

(a) To get personal satisfaction from developing my interests in art
(b) To learn a hobby
(c) To supplement my high school studies
(d) To get a job in the field of art using my artistic skills
(e) To do my current job in the field of art better
(f) To increase my appreciation or understanding of art
(g) Other:
(Please Describe) ______________
____
____

7. After you signed up for the AIS course, did you ever make a sincere and good faith effort to get a job using your artistic skills in the field of art?
   Yes ( ) No ( )
   (If "yes", skip to question 9; if "no", please answer question 8.)
8. Answer this question ONLY if you answered question 7 "no".) Please give the

most important reason why you did *not* try to get a job in the field of art. (Read all reasons first before you check *ONE.*)

(a) I took the course for advancement or improvement in my current job and not to get a new job in the field of art using my artistic skills, and I either;
(i) Got improvement or advancement; or
(ii) Did not get improvement or advancement
(b) I took the course mainly for self-improvement or self-fulfillment
(c) I preferred, already had, or got a job in another field unrelated to art
(d) I decided I didn't want a job in the field of art
(e) I decided I wouldn't be able to find a job in the field of art using my artistic skills since I had no on-the-job experience
(f) I decided I wouldn't be able to find a job in the field of art using my artistic skills since I hadn't enough training
(g) I decided I wouldn't be able to find a job in the field of art using my artistic skills because there was no demand for my talents
(h) I married or started a family
(i) I was drafted or enlisted in the military service
(j) I was going to high school or went on to college, vocational-technical, or other schooling
(k) I never wanted a job in the field of art in the first place
(l) Art is a hobby or recreational activity with me
(m) Other:
(Please Describe) ________________
____
____

9. (Answer this question ONLY if your answer to question 7 is "yes".) Did you ever get a job in the field of art or sell a substantial amount of free lance art work as a result of your training at Art Instruction School?
Yes ( ) No ( )
10. Do you feel that the course was worthwhile to you?
Yes ( ) No ( )
11. Would you recommend the course you took to a friend?
Yes ( ) No ( )
12. (a) What was your age when you signed up for the Art Instruction School course? ________________
(b) What is your age today? ________________
13. What was your job or main activity when you signed up for the course (such as "high school student", or "mechanic" or "housewife")? ______
____
14. Please attach to this form copies of any documents, if available, that show you paid any amount of money for any course of instruction offered by Art Instruction Schools.

This form must be signed and mailed in the enclosed self-addressed return envelope.

I CERTIFY THAT THE ABOVE ANSWERS ARE TRUE AND CORRECT TO THE BEST OF MY KNOWLEDGE AND BELIEF.

[Note: It is a federal crime for anyone to knowingly and willfully make a false, fictitious or fraudulent statement or representation in any matter within the jurisdiction of any department or agency of the United States. 18 U.S.C. Section 1001.]

________________________________ ________________________________
DATE STUDENT'S SIGNATURE

SOCIAL SECURITY NUMBER	PRINT NAME HERE

HOME ADDRESS:
Number Street Apt.
City State Zip Code

HOME TELEPHONE:

BUSINESS ADDRESS:

Employer's Name
Number Street
City State Zip Code

BUSINESS TELEPHONE:

Appendix E

Subject: Your enrollment in Art Instruction Schools, Inc. ("AIS") Minneapolis, Minnesota.

1. Is your current address correctly shown on the envelope?
   Yes ( ) No ( ) If not, what is your address?
2. (a) About when did you sign up for the AIS course?
   Month and Year
   (b) About when did you make your first payment to AIS?
   Month and Year
3. What was the name of the course?
4. (a) Did you finish the course you signed up for?
   Yes ( ) No ( )
   (b) If you dropped out of the course, about when did you do so?
   Month and Year
   (c) How many lessons of the total course did you finish?
   Total lessons finished ______
   Total lessons in course ______
5. As of today what is the total amount of money you have actually paid to AIS for your course?
   Total amount paid: $______
6. People take a corresondence course for various reasons. Which *one* of the reasons listed best fits your own reasons for taking the art course? (Read all reasons first before you check *ONE.*)

(a) To get personal satisfaction from developing my interests in art
(b) To learn a hobby
(c) To supplement my high school studies
(d) To get a job during the course in the field of art using my artistic skills
(e) To do my current job in the field of art better

(f) To increase my appreciation or understanding of art
(g) Other:
(Please Describe) ________________

____

____

7. After you signed up for the AIS course, did you ever make a sincere and good faith effort to get a job using your artistic skills in the field of art?
Yes ( ) No ( )
(If "yes", skip to question 9; if "no", please answer question 8.)
8. (Answer this question ONLY if you answered question 7 "no".) Please give the *most important* reason why you did *not* try to get a job in the field of art. (Read all reasons first before you check *ONE.*) (CHECK ONE ONLY)
(a) I took the course for advancement or improvement in my current job and not to get a new job in the field of art using my artistic skills, and I either;
(i) Got advancement or improvement; or
(ii) didn't get advancement or improvement
(b) I took the course mainly for self-improvement or self-fulfillment
(c) I preferred, already had, or got a job in another field unrelated to art
(d) I decided I didn't want a job in the field of art
(e) I decided I wouldn't be able to find a job in the field of art using my artistic skills since I had no on-the-job experience
(f) I decided I wouldn't be able to find a job in the field of art using my artistic skills since I hadn't enough training
(g) I decided I wouldn't be able to find a job in the field of art using my artistic skills because there was no demand for my talents
(h) I married or started a family
(i) I was drafted or enlisted in the military service
(j) I was going to high school or went on to college, vocational-technical, or other schooling
(k) I never wanted a job in the field of art in the first place
(l) Art is a hobby or recreational activity with me
(m) Other:
(Please Describe) ________________

____

____

9. (Answer this question ONLY if your answer to question 7 is "yes".) Did you ever get a job in the field of art or sell a substantial amount of free lance art work as a result of your training at Art Instruction School?
Yes ( ) No ( )
10. Do you feel that the course was worthwhile to you?
Yes ( ) No ( )
11. Would you recommend the course you took to a friend?
Yes ( ) No ( )
12. Please give the most important reason why you dropped the AIS course. (Read all reasons first before you check *ONE.*) (CHECK ONE ONLY)
(a) I gained the self-improvement I wanted when I signed up
(b) I felt I didn't have enough time for my art lessons because of my other activities or studies
(c) I found the course too difficult
(d) I didn't feel the course was worthwhile
(e) I didn't feel the course would help me get a job in the field of art
(f) I went to college or vocational-technical school

(g) I simply lost interest in studying art
(h) I could no longer afford the payments for the course
(i) Other:
(Please describe) ________________

____

____

13. (a) What was your age when you signed up for the Art Instruction School course? ________________
(b) What is your age today? ________________
14. What was your job or main activity when you signed up for the course (such as "high school student", or "mechanic" or "housewife")? ________________

____

15. Please attach to this form copies of any documents, if available, that show you paid any amount of money for any course of instruction offered by Art Instruction Schools.

This form must be signed and mailed in the enclosed self-addressed return envelope.

I CERTIFY THAT THE ABOVE ANSWERS ARE TRUE AND CORRECT TO THE BEST OF MY KNOWLEDGE AND BELIEF.

[Note: It is a federal crime for anyone to knowingly and willfully make a false, fictitious or fraudulent statement or representation in any matter within the jurisdiction of any department or agency of the United States. 18 U.S.C. Section 1001.]

________________________________ ________________________________

DATE STUDENT'S SIGNATURE

________________________________ ________________________________

SOCIAL SECURITY NUMBER PRINT NAME HERE

HOME ADDRESS:

____

Number Street Apt.

____

City State Zip Code

HOME TELEPHONE:

____

BUSINESS ADDRESS:

____

Employer's Name

____

Number Street

____

City State Zip Code

BUSINESS TELEPHONE:

____

IN THE MATTER OF

NATIONAL SYSTEMS CORPORATION, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF THE FEDERAL TRADE COMMISSION ACT

Docket 9078. Complaint, March 25, 1976 — Decision, Jan. 11, 1979

This consent order, among other things, dismisses the complaint against National Systems Corporation and individually named corporate officers, and requires North American Correspondence Schools, a Newport, Calif. firm offering correspondence courses in various fields, to cease misrepresenting enrollment prerequisites; school accreditation; testimonials; and the potential earnings, employment opportunities, and demand for its graduates. Prior to contracting, customers must be furnished with information regarding the employment success of former students; informed of their right to cancellation and refund; and provided with a seven-day cooling-off period. The order additionally requires the company to make restitution to former eligible students in a specified manner; maintain records; and institute a surveillance program designed to ensure compliance with the terms of the order.

Appearances

For the Commission: *Lani M. Sen Woltmann* and *Kendall H. MacVey.*

For the respondents: *Robert A. Skitol* and *Robert M. Cohan, Wald, Harkrader & Ross,* Washington, D.C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that National Systems Corporation, a corporation, and North American Correspondence Schools, a corporation and subsidiary of National Systems Corporation doing business as North American School of Conservation, North American School of Advertising, North American School of Drafting, North American School of Travel, North American School of Systems and Procedures, North American School of Recreation and Park Management, North American School of Surveying and Mapping, North American School of Accounting, North American School of Motorcycle Repair, and North American School of Hotel-Motel Management, and John J. McNaughton, individually and as chairman of the board of directors of National Systems Corporation, Maurice H. Sherman, individually and as an officer of North American Correspondence Schools, Richard C. Parsons and Eugene Auerbach, individually and as employees of North American Correspondence Schools, Wallace O. Laub, individually, as a member of the board of directors of North American Correspondence Schools, hereinafter sometimes referred to as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent National Systems Corporation is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware with its principal place of business located at 4361 Birch St., Newport Beach, California.

Respondent North American Correspondence Schools is a corporation and subsidiary of National Systems Corporation, organized, existing and doing business under and by virtue of the laws of the State of California with its principal office and place of business located at 4500 Campus Drive, University Plaza, Newport Beach, California.

Respondent John J. McNaughton was formerly president of National Systems and is now chairman of its Board of Directors and a member of the Board of Directors of North American Correspondence Schools. Respondent Maurice Sherman is president of North American Correspondence Schools. Respondent Eugene Auerbach is Director of Education for North American Correspondence Schools. Respondent Richard C. Parsons is an employee of North American Correspondence Schools. Respondent Wallace O. Laub is a member of the board of directors of North American Correspondence Schools. Together they formulate, direct, and control the acts and practices of North American Correspondence Schools, including the acts and practices hereinafter set forth. The address of Maurice Sherman and Richard Parsons is 4401 Birch St., Newport Beach, California. The address of Eugene Auerbach, Wallace O. Laub and John J. McNaughton is 4361 Birch St., Newport Beach, California.

PAR. 2. Respondents are now, and have been for some time last past, engaged in the advertising, offering for sale, sale and distribution of courses of instruction purporting to prepare students thereof for employment as game wardens, forestry aides, fish hatcherymen, soil conservation officers, government hunters, and various other positions associated with conservation and various positions in other fields of employment.

PAR. 3. In the course and conduct of their business as aforesaid, respondents now cause, and for some time last past have caused, said aforementioned courses of instruction to be distributed from their place of business in the State of California to purchasers thereof

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located in various other States of the United States. Respondents utilize the services of salesmen throughout the various states to induce the purchase of respondents' courses. Said salesmen transmit to and receive from respondents contracts, checks and other instruments of commercial nature. Respondents maintain, and at all other times mentioned herein have maintained, a substantial course of trade in said products in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 4. In the course and conduct of their aforesaid business, and for the purpose of inducing the purchase of their courses of instruction, respondents have made, and are now making, numerous statements and representations to prospective purchasers by way of the United States mail, radio, television, magazines, newspapers, and other forms of advertising, and in oral sales presentations made by their salesmen with respect to the availability of jobs and projections of occupational demand in the conservation field, or other fields of endeavor for which respondents purport to train their students, the degree which aforementioned courses of instruction enable persons to obtain employment, the starting and potential salaries and entry level of such jobs that are available, and the purpose of the salesmen's calls or solicitations.

Typical and illustrative of said statements and representations, but not all inclusive thereof, are the following:

A. Newspaper, Magazine and Direct Mail Advertisements

Ten Year Prediction of Manpower Needs in Conservation 1970–1980: Ecology, Up 180%; Forestry, Up 48%; Forestry Aids (sic), Up 83%; Range Management, Up 34%; Soil Conservation, Up 16%; Wildlife Conservation, Up 34%; Fishing Conservation, Up 67%; Environmental Protection, Up 260%. 425,810 more outdoor careers . . . millions of dollars more federal and state appropriations for acquiring new areas, building new facilities, hiring more conservationists.

* * * * * * *

Conservation is a growing movement in which thousands of people are finding helpful and satisfying careers.

* * * * * * *

Exciting job openings now for qualified men who love outdoor work.

* * * * * * *

Conservation And Ecology . . . a never ending need.

* * * * * * *

Many [conservation agencies] accepting applications now. Fine starting pay usually with regular advances.

* * * * * * *

. . .we show you how to seek exciting outdoor positions.

* * * * * * *

But the amazing part about outdoor jobs is that in many cases they actually pay off in gunny sacks of money.

* * * * * * *

Free Facts Mail Coupon on how to become a Game Warden, government hunter, forestry aid (sic), fish-wildlife manager or technician type positions that require less formal education.

* * * * * * *

Age limit 17–45, sometimes older on luxurious game farms and hunt clubs.

* * * * * * *

Wear the badge of the future in conservation . . . easy home study plan prepares you now for an outdoor man's dream career in forestry, wildlife, and soil conservation in ecology. (This text is set out in conjunction with pictures of game warden, soil conservationist, forestry aide, government hunter, and fish hatcheryman badges.)

* * * * * * *

Picture yourself in one of these exciting outdoor jobs. . . . (This text is set out in conjunction with photographs labeled game warden, forestry aide, fish hatcheryman, soil conservation officer and game club manager.)

* * * * * * *

Most conservation careers combine security with fine starting pay and regular advances.

* * * * * * *

B. Testimonials Used in Printed Advertisements

In April I became a Conservation Officer—1st Grade. I will be enforcing the fish and game laws of our State. Your Course helped make this life-long ambition a reality.

* * * * * * *

The NASC course paid off before I finished it. I know for a fact that just being a student. . .contributed toward my becoming a permanent park warden at Lake Louise District of Banff National Park.

* * * * * * *

North American School of Conservation has paid off for me. I now hold the title of

State Conservation Director of North Carolina for the National Campers and Hikers Association. Also I am a member of the Conservation Council of North Carolina.

* * * * * * *

I competed in an examination for park manager of the city of El Paso and won the position. I do not believe that I could have gotten the job without the training that I received from NASC. Thanks.

* * * * * * *

Lands Job First Day After Graduation. 'I finished my lesson and examination on Sunday and Monday I began work for the California Department of Fish and Game. This is what I consider fast results.

* * * * * * *

"I am encouraged by the level of work that N.A.S.C. is doing." Steward L. Udall, Former Secretary of the Interior Dept.

* * * * * * *

C. Television and Radio Advertisements

When you train for work as a game warden, wildlife manager, or government hunter you can forget about strikes and layoffs. . . .work outdoors—and get good pay, plus security and retirement. Call today for career information on how to train at home and qualify for an outdoor job.

* * * * * * *

If you are looking for a career that offers prestige and adventure . . . discover the opportunities that may await you in a conservation career. . . . And, it can all begin for you right here. . .at the famed North American School of Conservation, in Newport Beach, California.

* * * * * * *

D. Oral Presentations

Respondents' sales representatives begin their sales presentations by identifying themselves as representatives of the school sent to determine the prospect's qualifications for enrollment. The prospect is told that only the Director of Education can accept him as a student; however, it is standard procedure for the Director to accept the salesman's recommendation to enroll a student and it is in the salesmen's monetary self-interest to enroll as many prospects as possible.

* * * * * * *

Respondents' sales representatives insinuate that the programs and courses offered by North American will directly qualify the prospect to become a professional conservationist and that many professional jobs are available.

* * * * * * *

The openings in conservation are unlimited.

* * * * * * *

Respondents' School of Conservation is recognized by state and federal conservation agencies.

* * * * * * *

Respondents' School of Conservation is an accredited institution of higher learning.

* * * * * * *

Credit for respondents' conservation course is transferable to accredited colleges.

* * * * * * *

Respondents' course of instruction will enable a person to secure conservation employment, notwithstanding his age, physical fitness, formal educational training, and job experience in the conservation field.

PAR. 5. By and through the use of the above-quoted statements and representations, and others of similar import and meaning, but not expressly set out herein, respondents have represented, and are now representing, directly or by implication, that:

1. There is an urgent need or demand for all or most of respondents' graduates in positions for which respondents represent they are training such persons.

2. Respondents have a reasonable basis from which to conclude that:

(a) there was at the time such representations were made, or

(b) there would be at the time that persons then enrolling graduated from respondents' courses,

an urgent need or demand for all or most of respondents' graduates in positions for which respondents represent they are training such persons.

3. The testimonials used in respondents' advertising reflect typical job opportunities awaiting graduates of respondents' schools.

4. The testimonials used in respondents' advertising are true.

5. Completion of respondents' course of instruction, by itself, will enable a person to secure employment in the field of conservation, or other fields of endeavor for which respondents purport to train their students, from government agencies or private institutions, associations or groups.

6. Respondents had a reasonable basis from which to conclude that:

(a) at the time such representations were made, a substantial number of respondents' graduates were being hired, or

(b) a substantial number of persons then enrolling in respondents' courses would upon graduation be hired,

by government agencies or private institutions, associations or groups in the positions for which respondents represent they are training such persons.

7. Graduates of respondents' course qualify for professional or technically skilled employment in conservation or other fields of endeavor for which respondents represent they are training such graduates.

8. Age, physical fitness, formal education training, or job experience are not important hiring considerations for conservation employment or other employment for which students are purportedly trained by respondents.

9. Graduates of respondents' courses will receive high salaries from employment in positions for which respondents represent they are training such graduates.

10. Respondents had a reasonable basis from which to conclude that:

(a) a substantial percentage of persons graduating from respondents' courses at the time such representations were made, were earning, or

(b) a substantial percentage of persons then enrolling in respondents' courses would earn when they graduated,

high salaries in positions they obtained as a result of respondents' training.

11. Enrollment in respondents' course is selective.

12. Respondents' qualification questionnaire is utilized to determine a prospect's enrollment qualifications.

13. Respondents' school is an accredited institution of higher learning and credit therefrom is transferable to accredited institutions of higher learning.

PAR. 6. In truth and in fact:

1. There is not an urgent need or demand for all or most of respondents' graduates in positions for which respondents represent they are training such persons.

2. Respondents had no reasonable basis from which to conclude that:

(a) there was at the time such representations were made, or

(b) would be at the time that persons enrolling graduated from respondents' courses,

an urgent need or demand for all or most of respondents' graduates in positions for which respondents represent they are training such persons.

3. The testimonials used in respondents' advertising do not reflect the typical job opportunities awaiting graduates of respondents' schools.

4. Some of the testimonials used in respondents' advertising are untrue; while others, because of omission of pertinent facts are deceptive.

5. Completion of respondents' course of instruction by itself will not enable a person to obtain conservation employment or other employment for which students are purportedly trained by respondents, from government agencies or private institutions, associations or groups.

6. Respondents had no reasonable basis from which to conclude that:

(a) at the time such representations were made, a substantial number of respondents' graduates were being hired, or

(b) a substantial number of persons then enrolling in respondents' courses would upon graduation be hired, by government agencies or private institutions, associations or groups in the positions for which respondents represent they are training such persons.

7. Completion of respondents' course of instruction will not qualify a person for professional or technically skilled conservation employment or other employment for which students are purportedly trained by respondents. Such positions often require a college degree or extensive job experience.

8. While employment qualifications vary from state to state, age, physical fitness, formal educational training and job experience are important hiring considerations for most conservation employment or other employment for which students are purportedly trained by respondents.

9. Graduates of respondents' courses will not necessarily receive high salaries from employment in positions for which respondents represent they train such graduates.

10. Respondents had no reasonable basis from which to conclude that:

(a) a substantial percentage of persons graduating from respondents' courses at the time such representations were made, were earning, or

(b) a substantial percentage of persons then enrolling in respondents' courses would earn when they graduated,

high salaries in the positions they obtained as a result of respondents' training.

11. Enrollment in respondents' course of instruction is not selective.

12. Respondents' qualification questionnaire is not utilized to

determine a prospect's enrollment qualifications. It is utilized as a promotional device to induce the purchase of respondents' course of instruction.

13. Respondents' school is not an accredited institution of higher learning and credit therefrom is not transferable to accredited institutions of higher learning.

Therefore, the statements and representations set forth in Paragraphs Four and Five were and are false, misleading, deceptive or unfair acts or practices.

PAR. 7. Respondents offered for sale courses of instruction which purported to prepare graduates thereof for available positions in the field of conservation and other fields of endeavor without disclosing in advertising or through their sales representatives: (1) the percentage of recent graduates for the course offered that were able to obtain employment in the positions for which they were allegedly trained; (2) the employers that hired any such recent graduates for the course offered; (3) the initial salary any such recent graduates from the course received; and (4) the percentage of recent enrollees of the school for the course offered that have failed to complete the course of instruction. Knowledge of such facts would indicate the probability of graduating from respondents' courses, of securing employment upon graduating and of the nature of such employment.

Thus, respondents have failed to disclose material facts, which, if known, would be likely to affect a prospective enrollee's consideration to purchase such courses of instruction. Therefore, the aforesaid acts and practices were, and are, false, misleading, deceptive or unfair acts or practices.

PAR. 8. Respondents, as aforesaid, have been, and are now failing to disclose material facts while using other false, misleading, deceptive or unfair acts or practices, to induce persons to pay over to respondents substantial sums of money to purchase courses of instruction which were of little use or value to the said persons in obtaining employment in the jobs for which they were trained. Respondents have received the said sums and have failed to offer to refund and have refused to refund such money to such purchasers of their courses.

The use by respondents of the aforesaid practices and their continued retention of the said sums, as aforesaid, is an unfair act or practice.

PAR. 9. By and through the use of the aforesaid acts and practices, respondents place in the hands of others the means and instrumentalities by and through which they mislead and deceive the public in the manner and as to the things hereinabove alleged.

PAR. 10. In the course and conduct of their business, and at all times mentioned herein, respondents have been and now are in substantial competition in or affecting commerce, with corporations, firms and individuals engaged in the sale of courses of instruction covering the same or similar subjects.

PAR. 11. The use by respondents of aforesaid false, misleading, unfair or deceptive statements, representations, acts and practices, has had, and now has, the capacity and tendency to mislead members of the purchasing public into the erroneous and mistaken belief that said statements and representations were and are true, and to induce a substantial number thereof to purchase respondents' said courses of instruction by reason of said erroneous and mistaken belief.

PAR. 12. The aforesaid acts and practices of respondents, as herein alleged, were and are all to the prejudice and injury of the public and of respondents' competitors and constituted, and now constitute, unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Commission having issued its complaint on March 25, 1976, charging respondents with violation of Section 5 of the Federal Trade Commission Act, and respondents having been served with a copy of that complaint; and

The Commission having duly determined upon a joint motion of complaint counsel and respondents' counsel that in the circumstances presented, the public interest would be served by withdrawal of the matter from adjudication pursuant to Section 3.25 of the Commission's Rules; and

The respondent North American Correspondence Schools and complaint counsel having executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, as amended, and waivers and other provisions as required by the Commission's Rules; and

The Commission having considered the agreement and having provisionally accepted same, and the agreement containing consent order having thereupon been placed on the public record for a period of sixty (60) days, now in further comformity with the procedure prescribed in Section 3.25(d) of its Rules, the Commission hereby makes the following jurisdictional findings, and enters the following order:

1. Respondent North American Correspondence Schools is a corporation and subsidiary of National Systems Corporation, organized, existing and doing business under and by virtue of the laws of the State of California with its principal office and place of business located at 4401 Birch St., Newport Beach, California.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

I

It is ordered, That respondent North American Correspondence Schools (hereinafter "respondent"), a corporation and a subsidiary of National Systems Corporation, doing business as North American School of Conservation, North American School of Advertising, North American School of Drafting, North American School of Travel, North American School of Systems and Procedures, North American School of Recreation and Park Management, North American School of Surveying and Mapping, North American School of Accounting, North American School of Motorcycle Repair, and North American School of Hotel-Motel Management, its successors and assigns, and respondent's officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division or other device, in connection with the advertising, promoting, offering for sale, sale or distribution of courses of instruction in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

1. Representing, orally, visually, in writing or in any other manner, directly or by implication that:

(a) There is a need or demand of any size, proportion or magnitude for persons completing any of the courses offered by respondent in the field of conservation or any other field, or otherwise representing that opportunities for employment, or opportunities of any size, figure or number are available to such persons, or that persons completing any such courses will or may earn any specified amount of money, or otherwise representing by any means the prospective earnings of such persons, unless respondent possesses, and relies upon at the time such representation is made, a reasonable basis for such representation, which may consist of a statistically valid and reliable survey, a reliable study, a government or industry publication or other data or material which would be relied upon by an individual generally recognized as qualified as an expert on the subject matter pertaining to the representation in question.

(b) Completion of respondent's courses of instruction in conservation by itself will enable a person to secure employment in conservation from government agencies or private institutions, associations or groups; or, misrepresenting in any manner the importance or significance of any of the courses offered by respondent for qualifying any person for employment in any field with any firms.

(c) Graduates of respondent's conservation courses qualify for employment in conservation of a kind normally requiring a junior or senior college degree; or, misrepresenting in any manner that persons completing any of the courses offered by respondent will qualify for employment of a kind normally requiring a junior or senior college degree.

(d) Graduates of respondent's conservation courses qualify for employment in conservation irrespective of age, physical fitness, formal educational training or job experience; or, misrepresenting in any manner the employment qualifications for conservation or any other field.

(e) Respondent's School of Conservation, or any other school of respondent, is an accredited institution of higher learning, or that credits therefrom are transferable to accredited institutions of higher learning, unless such is the case.

(f) Respondent's courses of instruction in conservation, or in any other field, are approved or recommended by any persons, groups, or organizations knowledgeable in the field of conservation, or in any other field, unless said persons, groups, or organizations have in fact approved or recommended such courses.

2. Representing orally, visually, in writing or in any other manner, including but not limited to the use of photographs or testimonials, the positions or salaries obtained by graduates of respondent's courses, or the employers who have hired such graduates, unless respondent possesses and relies upon at the time such representation is made, a reasonable basis for such representation, which may consist of a statistically valid and reliable survey, a reliable study, a government or industry publication or other data or material which would be relied upon by an individual generally recognized as qualified as an expert on the subject matter pertaining to the representation in question.

3. Altering or omitting any part of the text of a testimonial used

in respondent's advertising in a manner which is likely to deceive members of the public as to the benefits to be obtained from any of the courses offered by respondent; or, misrepresenting in any manner the content of any testimonial used by respondent in any of its advertising.

4. Failing to state, clearly and conspicuously, in conjunction with any testimonial used in respondent's advertising, that it has been solicited, or is required, as part of the course work, or that the entity giving such testimonial has received remuneration therefor, when such is the case.

5. Failing to obtain, at least twenty-four (24) hours prior to an interview or visit in the home or residence of a prospective student, the prospective student's consent to an interview or visit in her (his) home; failing to disclose to said prospective student, at the outset of any telephone call or other contact intended to solicit her (his) consent to an interview or visit in her (his) home, that the purpose of the contact is to request an opportunity to interview or visit the prospective student at her (his) home, and that the purpose of such interview or visit would be to sell an enrollment in one of the courses of instruction offered by respondent.

6. Failing to disclose, in writing, clearly and conspicuously, prior to the signing of any contract, to any prospective student of any course of instruction offered by respondent, the following information in the format prescribed in Appendix A:

(a) the percentage of graduates from respondent's course available for employment and employed in the field to which the course relates, as shown by respondent's most recent survey conducted in the manner required or approved by the Veterans Administration (VA) pursuant to 38 U.S.C. 1673 and 1723, as amended, and all applicable regulations and circulars; and

(b) the percentage of students in respondent's course during the time period covered by the VA survey used as the basis for the disclosure required by subparagraph (a) of this paragraph who, after having commenced the course, cancelled their enrollment or were terminated by respondent before completion of the course.

Provided, however, that this paragraph shall be inapplicable:

(a) to any school newly established by respondent in a metropolitan area or county, whichever is larger, where it previously did not operate a school, until such time as the school has graduated the number of students sufficient to conduct a valid survey under the applicable VA regulations and circulars and has conducted such a survey at the earliest possible time; or

(b) to any course newly introduced by respondent, until such time as the course has graduated the number of students sufficient to conduct a valid survey under the applicable VA regulations and circulars and has conducted such a survey at the earliest possible time; or

(c) to any school or course of instruction whose advertising or marketing does not entail employment or earnings claims.

However, in the instance of (a) and (b) above, the following statement, and no other, shall be made in lieu of the Appendix A Disclosure Form required by this paragraph:

DISCLOSURE NOTICE

THIS SCHOOL [OR COURSE, AS THE CASE MAY BE] HAS NOT BEEN IN OPERATION LONG ENOUGH TO INDICATE WHAT, IF ANY, ACTUAL EMPLOYMENT OR SALARY MAY RESULT UPON GRADUATION FROM THIS SCHOOL [COURSE].

7. (a) Contracting for the sale of any course of instruction in the form of a sales contract or any other agreement which does not contain in close proximity to the space reserved in the contract for the signature of the prospective student, in a clear and concise manner, and in type that is readable and conspicuous and not smaller than the majority of type used on the enrollment form, the following statement:

You may cancel this transaction at any time prior to midnight of the seventh (7th) calendar day after the date you sign this contract. See enclosed notice of cancellation form for an explanation of this right.

(b) Failing to furnish each prospective student, at the time she (he) is furnished the enrollment contract, a complete form enclosed immediately after the enrollment contract, containing the following information and statements:

NOTICE OF CANCELLATION

You may cancel this transaction, without any penalty or obligation, within seven (7) calendar days from the date you sign the enrollment application.

If you cancel, any payments made by you under the contract or sale, and any note or other evidence of indebtedness executed by you will be returned within seven (7) calendar days following receipt by the school of your cancellation notice, and any security interest arising out of the transaction will be cancelled. If you cancel, the school may ask that you return any materials delivered to you as part of the course, at the school's expense and risk.

To cancel this transaction, sign, date and mail or deliver this cancellation notice or any other written notice, or send a telegram to North American Correspondence

Schools at [address] not later than midnight of the seventh (7th) calendar day after you sign the enrollment application.

I HEREBY CANCEL THIS TRANSACTION.

(Date) *(Student's signature)*

(c) Where a sales representative is involved in the enrollment process, failing to inform orally each prospective student of her (his) right to cancel at the time she (he) signs a contract or agreement for the sale of any course of instruction.

(d) Misrepresenting in any manner the prospective student's right to cancel.

(e) Failing or refusing to honor any valid notice of cancellation by a prospective student and, within seven (7) calendar days after the receipt of such notice, to: (i) refund all payments made under the contract or sale and return any check not cashed or deposited; (ii) return any goods or property traded in, in substantially as good condition as when received by respondent; (iii) cancel and return any note or other evidence of indebtedness executed by the prospective student in connection with the contract or sale.

(f) During the cancellation period described herein, respondent shall not initiate oral contacts with such contracting persons other than contacts permitted by this paragraph, and such contracting persons shall not receive any written materials from respondent before expiration of the cancellation period.

(g) *Provided, however,* that the above statement and cancellation notice may be omitted from enrollment contracts signed during or following an interview or sales presentation in a person's home or residence by a sales representative if, in such circumstances, respondent complies with Paragraph I(8) of this order.

8. Failing to mail, by certified mail return receipt requested, to each person who signs an enrollment contract during or immediately following an interview or sales presentation in her (his) home or residence by a sales representative, a form in duplicate, printed in boldface type of at least ten (10) points and containing the following language:

AFFIRMATION STATEMENT

The enrollment contract that you have signed with North American School of ________________ on [date] to enroll in [name of course] is not effective or valid unless you first sign this statement and mail it to the school within ten (10) days from the time that you received this statement. You are free to cancel your enrollment and receive a full refund of any monies you have paid to the school by not signing or mailing this statement within ten (10) days. At the expiration of this ten (10) day period the school has ten (10) business days to send you your refund (if any) and to cancel and return to you any evidence of indebtedness that you signed. However, if you want to enroll in the school, you should sign your name below and mail this statement to the school within ten (10) days. Keep the duplicate copy for your own records.

I want to enroll in the North American School of ________________ .

(Date) *(Signature)*

9. Failing to inform orally each person interviewed or visited at home or in such person's residence by a sales representative, in the course of any such interview or visit, that any enrollment contract signed by such person will not be effective or valid unless and until that person signs and mails an Affirmation Statement that she (he) will receive from the school in the mail, and that she (he) is free to cancel the contract by simply not mailing the Affirmation Statement back to the school within ten (10) days of its receipt.

10. Treating any enrollment contract signed during or immediately following an interview or sales presentation in a person's home or residence by a sales representative as effective or valid, or sending course materials to any such person, unless and until the Affirmation Statement described in Paragraph I(8) of this order is signed and mailed within the prescribed affirmation period; failing to treat any such contract for which an Affirmation Statement is not signed and mailed within the affirmation period as null and void; and failing within ten (10) business days of the expiration of the affirmation period, to return all monies received, and to cancel and return all evidence of indebtedness, relating to any such unaffirmed contract.

11. Representing orally through sales representatives that respondent accepts only qualified candidates for enrollment in its conservation courses; or misrepresenting in any manner the prerequisites or qualifications for enrollment in any of the courses of instruction offered by respondent.

12. Representing orally through sales representatives that respondent's qualification questionnaire is utilized to determine a prospective student's enrollment qualifications; or misrepresenting in any manner the purpose or use of respondent's qualification questionnaire.

13. Furnishing or otherwise placing in the hands of others the means and instrumentalities by and through which the public may

be misled or deceived in the manner, or by the acts and practices, prohibited by this order.

II

1. *It is further ordered,* That:

(a) Respondent herein deliver a copy of this decision and order to each of its sales representatives, and to all personnel having oral contact with prospective students of the courses offered by respondent or otherwise directly engaged in the promotion, offering for sale, sale or distribution of any course of instruction included within the scope of this order;

(b) Respondent herein provide each person so described in subparagraph (a) of this paragraph with a form returnable to the respondent clearly stating her (his) intention to conform her (his) business practices to the requirements of this order; retain said statement during the period said person is so engaged; and make said statement available to the Commission's staff for inspection and copying upon request;

(c) Respondent herein inform each person described in subparagraph (a) of this paragraph that respondent will not use or engage, or will terminate the use or engagement of, any such person unless such person agrees to and does file notice with the respondent that she (he) will conform to the provisions contained in this order;

(d) If a person described in subparagraph (a) of this paragraph will not agree to file the notice set forth in subparagraph (b) above with the respondent and conform to the provisions of this order, the respondent shall not use or engage or continue the use or engagement of such person to promote, offer for sale, sell or distribute any course of instruction included within the scope of this order;

(e) Respondent herein inform the persons described in subparagraph (a) above that the respondent is obligated by this order to discontinue dealing with or to terminate the use or engagement of persons who continue on their own the deceptive acts or practices prohibited by this order;

(f) Respondent herein institute a program of continuing surveillance designed to reveal whether the business practices of each said person described in subparagraph (a) above conform to the requirements of this order;

(g) Respondent herein discontinue dealing with or terminate the use or engagement of any person described in subparagraph (a) above, who continues on her (his) own any act or practice prohibited by this order as revealed by the aforesaid program of surveillance;

(h) Respondent herein maintain files containing all inquiries or complaints from any source relating to acts or practices prohibited by this order, for a period of two (2) years after their receipt, and that such files be made available for examination by a duly authorized agent of the Federal Trade Commission during the regular hours of the respondent's business for inspection and copying.

2. *It is further ordered,* That respondent herein present to each interested applicant or prospective student immediately prior to the commencement of any interview or sales presentation during which the purchase of or enrollment in any course of instruction offered by respondent herein is discussed or solicited in such person's home or residence, a 5" x 7" card containing only the following language:

YOU WILL BE TALKING TO A SALESPERSON.

3. *It is further ordered,* That respondent forthwith distribute a copy of this order to each of its operating divisions.

4. *It is further ordered,* That respondent shall, for a period of twenty (20) years following the effective date of this order, notify the Commission at least thirty (30) days prior to any proposed change in the corporate structure of respondent such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the respondent which may affect compliance obligations arising out of this order.

5. *It is further ordered,* That should the Federal Trade Commission promulgate a trade regulation rule governing the advertising or promotion of educational courses of instruction subject to this order, provisions of this order relating to practices, requirements or prohibitions covered by such a rule shall automatically be replaced by the provisions of such a rule relating to the same kind of practices, requirements or prohibitions, to the extent covered by such provisions, and any such replacement provisions of the rule shall be incorporated in this order, on the date such rule becomes effective; but shall remain so incorporated only as long as the rule remains effective. If such replacement provisions of the rule should be rescinded or otherwise invalidated, the original provisions of the order herein shall then become effective.

III

It is further ordered, That:

1. Within twenty-one (21) days after the date this order is served on respondent (hereinafter "date of service"), respondent shall

employ an independent contractor (hereinafter "contractor") acceptable to the Commission.

2. Within thirty (30) days after the date of service, respondent shall compile and give to the contractor a list containing the information described in this paragraph. For each person (a) whose enrollment application was accepted and registered by respondent for any of respondent's conservation courses [whether consisting of one hundred and fifty (150) or one hundred (100) lessons; hereinafter "the course"] from March 26, 1973, through March 25, 1976, inclusive; and, (b) who, on or before June 30, 1977, either (1) completed all the lessons in the course (but need not have submitted the final examination or received a diploma) and paid in full the tuition for the course, or (2) cancelled the course or was terminated by the school [for academic reasons or because of lack of communication from the student for two hundred and twenty (220) days] after having completed at least ten (10) examinations in the course and paid at least the pro rata portion of the tuition attributable to ten (10) examinations, (hereinafter "student"), respondent shall provide the following information:

(a) Name;

(b) Last known home address;

(c) Name and address of the nearest relative of the student, or if no such address appears in respondent's files relating to such student, then the student's last known business address if such information is contained in respondent's files relating to such student;

(d) Date student's enrollment application was accepted and registered by respondent;

(e) Date student completed the course (but need not have submitted a final examination or received a diploma) *or* date she (he) cancelled the course or was terminated by respondent for academic reasons or for failure to communicate with respondent for two hundred and twenty (220) days;

(f) Total tuition paid by or for the student to respondent;

(g) Total amount of any tuition refund(s) paid by respondent to the student;

(h) Total amount of any deficiency in the student's pro rata tuition payments; and

(i) If known, the total amount of tuition paid on behalf of, or reimbursed to, the student by any government agency or department (other than the Veterans Administration), or any private business or other organization.

3. On the sixtieth (60th) day after the date of service, the contactor shall send, via first class mail, to each student at her (his)

last known home address (as it appears in the section of the list referred to in Paragraph III(2)(b) of this order) an envelope which bears the contractor's return address and contains:

(a) A copy of the letter and the Eligibility Questionnaire (hereinafter "questionnaire") in the language, manner and form shown in Appendices B and C respectively; and

(b) A first class postage-prepaid envelope addressed to the contractor.

4. With respect to each student whose mailed inquiry (as described in Paragraph III (3)) is returned to the contractor undelivered or from whom no response has been received within one hundred and five (105) days after the date of service, then, within one hundred and ten (110) days after the date of service, the contractor shall do either of the following:

(a) solicit a more recent address by sending via first class mail to the name and address of the student's nearest relative shown on the list referred to in Paragraph III(2), an envelope which bears the contractor's return address and contains both a letter in the language, manner and form shown in Appendix D and a first-class postage-prepaid envelope addressed to the contractor; if informed of an address more recent than the address referred to in Paragraph III(2), then within five (5) business days of receiving said address, the contractor shall send, via first class mail, to the student at said address, an envelope bearing the contractor's return address and containing the same letter, questionnaire and return envelope referred to in Paragraph III(3) of this order; or

(b) if there is no name or address of a relative on the list referred to in Paragraph III(2), send via first class mail to the student's last known business address if and as it appears on said list an envelope bearing the contractor's return address and containing the same letter, questionnaire and return envelope that were previously mailed to the student's home address.

5. (a) On the one hundred and fifth (105th) day after the date of service, the contractor shall transmit to the Commission a list containing the name of each student whose envelope is returned to the contractor, or from whom no response has been received within one hundred and five (105) days after the date of service, and for whom neither a business address nor a relative's address appears on the list referred to in Paragraph III(2) of this order;

(b) The Commission shall have up to one hundred and forty-five (145) days from the date of service to obtain and transmit to the contractor more recent addresses for the students whose names appear on the list described in Paragraph III(5)(a) of this order;

(c) With respect to each student for whom a more recent address is transmitted to the contractor by the Commission pursuant to the provisions of Paragraph III(5)(b) of this order, the contractor shall, on the one hundred and fiftieth (150th) day after the date of service, send, via first class mail, an envelope which bears the contractor's return address and contains the questionnaire, letter and return envelope described in Paragraph III(3)(a) and (b) of this order.

6. If a student marks more than one answer to questions 2 and/or 4 (see Appendix C) when at least one answer would be a qualifying answer and the other a disqualifying answer under the eligibility criteria enumerated in Paragraph III(8)(a–e) in this order, and if the student is not disqualified on the basis of an answer to any other question, the contractor within five (5) days shall send to such student via first class mail an envelope bearing the contractor's return address and containing: a letter as depicted in Appendix E; an unmarked copy of the question(s) to which the student had given inconsistent answers; and a first-class postage-prepaid envelope addressed to the contractor.

7. On the two hundredth (200th) day after the date of service, the contractor shall transmit to respondent and to the Commission a copy of each completed questionnaire in the contractor's possession, custody, or control. No student whose questionnaire is received by the contractor after that day will be considered for eligibility.

8. Within two hundred and ten (210) days after the date of service, the contractor shall make an initial determination of those students who are "eligible class members" pursuant to the criteria enumerated in this paragraph, Paragraph 9 and the guidelines set forth in Appendix H of this order, and shall transmit to the respondent and to the Commission a list of the names of students who are eligible class members and the most current address for each such student known to the contractor. An "eligible class member" is defined as that person:

(a) whose enrollment application was accepted and registered by respondent between March 26, 1973 and March 25, 1976, inclusive;

(b) who enrolled in the course to enable her (him) to get a job in the conservation or ecology field;

(c) who failed to obtain employment in the conservation or ecology field (1) within two (2) years after completing or terminating the course, or (2) by the date of receipt of the questionnaire, whichever is earlier;

(d) who has demonstrated her (his) eligibility by her (his) responses to the questionnaire and any subsequent questionnaire or inquiry mailed by the contractor pursuant to the provisions of this order; and the contractor has received all such responses before two hundred (200) days after the date of service; and

(e) who falls into one of the following groups:

(1) that person who completed all the lessons in the course (but may not have submitted the final examination or been issued a diploma), and paid in full the tuition for the course on or before June 30, 1977, and made three (3) "meaningful attempts" (as defined in Paragraph 9) to find a job in the conservation or ecology field at least one (1) of which was either a written application for a job or a personal visit to an agency or employer for the purpose of finding a job; or

(2) that person who cancelled her (his) enrollment in the course or was terminated by respondent (for academic reasons or because of lack of any communication from the student for two hundred and twenty (220) days) and made at least two (2) "meaningful attempts" (as defined in Paragraph 9) to find a job in the conservation or ecology field.

9. For the purposes of Paragraph III(8)(e)(1) and (2), a "meaningful attempt" to find a job in the conservation or ecology field is one in which the student:

(a) Filed a written application for employment with an agency or other employer in the conservation or ecology field, and can reasonably identify the agency or employer to which, and the approximate date on which, application was made;

(b) Wrote to an agency or employer in the conservation or ecology field to inquire about employment but did not file a written application for employment, and can reasonably identify the agency or employer to which, and the approximate date on which, the inquiry was sent;

(c) Contacted the North American School of Conservation for assistance in getting a job in the conservation or ecology field;

(d) Telephoned an employer in the conservation or ecology field to inquire about the availability of a conservation or ecology job but failed to apply for a conservation or ecology job because (1) she (he) was ineligible to apply, (2) she (he) chose not to apply because the salary was too low, or (3) she (he) was advised that no jobs were available; and can reasonably identify the agency or employer contacted and the approximate date of the contact; or

(e) Personally visited an employer in the conservation or ecology field to inquire about the availability of a conservation or ecology job but failed to apply for a conservation or ecology job because (1) she (he) was ineligible to apply, (2) she (he) chose not to apply because the salary was too low, or (3) she (he) was advised that no jobs were available; and can reasonably identify the agency or employer contacted, the person to whom she (he) spoke (name, position, title or description), and the approximate date of the contact.

10. Within two hundred and forty (240) days after the date of service, respondent shall present to the contractor any challenge respondent may wish to make to the contractor's initial determinations of eligibility, and respondent shall present to the contractor simultaneously with its challenge any substantiating materials in its possession, custody, or control. On the same day that respondent presents its challenges to the contractor, it shall transmit copies of all challenges and substantiating materials constituting said presentation to the Commission.

11. (a) Within two hundred and seventy (270) days after the date of service, the contractor shall, after considering all of respondent's challenges to the contractor's initial determinations of eligibility, make its final determinations of those students who are eligible class members. Also within two hundred and seventy (270) days after the date of service, the contractor shall notify respondent and the Commission simultaneously of said final determinations by transmitting to each of them a list of the names and most current addresses of students who are eligible class members, a report explaining the basis for upholding or denying any challenge(s) and copies of all materials considered by the contractor in upholding or denying any challenge.

(b) In resolving disputes about whether particular students are eligible class members, the contractor shall consider all evidence presented to it that bears on the appropriateness and reasonableness of the contractor's interpretation of responses to the questionnaire and all evidence presented to it that bears on the accuracy or veracity of a student's responses to the questionnaire pursuant to the guidelines set forth in Appendix H of this order. The contractor's decision in upholding or denying any challenge shall be fair and impartial. No financial or other material benefit shall accrue to the contractor contingent upon the nature of the outcome of her (his) decision.

12. Within two hundred and eighty (280) days after the date of service, respondent shall file, under Rule 3.61(d) of the Commission's Rules of Practice, a written request for advice as to whether the contractor's final determinations of eligible class members comply with the terms of this order. The Commission shall render its advice to respondent within three hundred and forty (340) days after the date of service.

13. Within three hundred and sixty-five (365) days after the date

of service, respondent shall send, via registered mail, return receipt requested, an envelope to each of the eligible class members at the address on the list prepared by the contractor pursuant to Paragraph III(11)(a) of this order containing a letter in the language, manner, and form shown in Appendix F and:

(a) In the case of a student who has completed all the lessons in the course (but may not have submitted the final examination or been issued a diploma) and paid in full the tuition for the course, on or before June 30, 1977, a check for the lesser of the following amounts:

(1) Two hundred dollars ($200.00);

(2) The amount by which the tuition paid by or for the student exceeds the amount paid on behalf of, or reimbursed to, the student by any government agency or department (other than the Veterans Administration) or any private business or other organization (excluding loans); or

(b) In the case of a student whose enrollment has been cancelled or terminated as described in Paragraph III(8)(e)(2) of this order, a check for the lesser of the following amounts:

(1) One hundred dollars ($100.00);

(2) The amount by which the tuition paid by or for the student exceeds the amount paid on behalf of, or reimbursed to, the student by any government agency or department (other than the Veterans Administration) or any private business or other organization;

provided, however, that if the student had not paid for all of the lessons completed prior to cancellation or termination of her (his) enrollment, the pro rata cost of the lessons she (he) completed but for which she (he) had not paid will be deducted from the refund to which she (he) is otherwise entitled.

14. On the same day that respondent mails envelopes containing refund checks to eligible class members, pursuant to Paragraph III(13) of this order, respondent shall send, via first class mail, an envelope which bears respondent's return address and contains a letter in the language, manner and form shown in Appendix G and a copy of this order to the last known home address of each student who was determined on the basis of her (his) returned questionnaire to be ineligible for a refund under Part III of this order.

15. On the four hundred and twenty-fifth (425th) day after the date of service, respondent shall file with the Commission a report in writing setting forth the manner and form in which it has complied with Part III of this order. This report shall contain a listing of the names, addresses, and refund amounts of those eligible class

members whose refund checks were returned by the United States Postal Service.

16. The Federal Trade Commission shall have one hundred and eighty (180) days from the date of receipt of the report described in Paragraph III(15) of this order to locate such eligible class members and to notify respondent of such members' most recent addresses, if found.

17. Within five (5) days of receiving the notification referred to in Paragraph III(16) of this order, respondent shall send, via registered mail, return receipt requested, an envelope to each of the eligible class members whom the Federal Trade Commission has located, at the address found by the Commission, which bears respondent's return address and contains the letter and check referred to in Paragraph III(13) of this order.

18. Any administrative costs incurred by respondent in carrying out the provisions of this Part III, including the cost of employing the contractor, shall be borne by respondent.

19. If any duty required to be performed on a certain day under Part III of this order falls upon a non-business day, the respondent herein shall perform such duty on the next following business day.

IV

It is further ordered, That:

1. Respondent shall maintain records and documents for two (2) years after the filing of the report referred to in Paragraph III(15) of this order, which demonstrate that respondent has complied with Part III of this order, and shall further maintain all documents and other materials relied upon in compliance with Parts I and II of this order for a period of two (2) years following the last date such documents and materials were relied upon. Such records, documents and materials demonstrating compliance with this order shall be made available for inspection and copying by the Commission during normal business hours.

2. In addition to all other reports required by this order, respondent shall file with the Commission within sixty (60) days after service upon it of this order, a report, in writing, setting forth in detail the manner and form in which it has complied with Parts I and II of this order.

3. The Complaint against National Systems Corporation, a Corporation; John J. McNaughton, individually and as chairman of the board of directors of National Systems Corporation; Maurice H. Sherman, individually and as an officer of North American Correspondence Schools; Eugene Auerbach and Richard C. Parsons,

individually and as employees of North American Correspondence Schools; and Wallace O. Laub, individually and as a member of the board of directors of North American Correspondence Schools, be, and it hereby is, dismissed.

APPENDIX A

DISCLOSURE FORM

(Name of School)

EMPLOYMENT AND COMPLETION RECORD FOR (NAME OF COURSE) FOR THE PERIOD OF (DATE) TO (DATE)

1. (Name of School) recently conducted a survey, pursuant to regulations of the Veterans Administration,[1] of students who graduated from the (name of course) between (date) and (date). (Number) questionnaires were mailed; (number) were returned. The survey shows that among the graduates who responded to the questionnaire, (percentage) of graduates available for employment actually obtained jobs in the (name of field) or a related field.

2. (Percentage) of the students who enrolled in (name of course) between (date) and (date) completed the course; (percentage) of the students who enrolled in that period cancelled their enrollment or were terminated by the school before completion of the course; (percentage) of the students who enrolled in that period are still studying the course.

APPENDIX B

(Name)
(Address)

Dear (Name):

In settlement of a proceeding brought by the United States Federal Trade Commission, North American Correspondence Schools has agreed to a Consent Order. Under that Order, North American is undertaking to make tuition adjustments for some former students of its Conservation course, if they meet certain requirements. The purpose of the enclosed questionnaire is to help determine your eligibility for such an adjustment.

You are under no obligation to fill out or send in this questionnaire. You must return this questionnaire, however, if you wish to have your eligibility determined. You may already have received and sent in other questionnaires relating to the Conservation course. Those questionnaires were used for other purposes and do not contain sufficient information to determine your eligibility.

DIRECTIONS: Please read each question carefully and mark or fill in the appropriate spaces on the questionnaire enclosed. After you have answered every applicable question, take the questionnaire to a notary public. Sign and swear to the Affidavit in the presence of the notary public, who will then notarize it. If you do not live within twenty-five (25) miles of a notary public, you may sign and swear to the Affirmation before three persons who are not related to you and who are at least

[1] [The following disclaimer shall be inserted if the course has not been approved by the Veterans Administration: "This course is not approved for veterans benefits."]

eighteen (18) years of age, each of whom must attest that he or she has witnessed your signing of the Affirmation statement.

If you decide to send in this questionnaire, you must follow the directions and answer all questions which apply to you completely and truthfully to the best of your knowledge. Questionnaires which are incomplete or improperly filled out could result in the loss of eligibility. Please keep in mind that you can be exposed to criminal penalties if you knowingly give false information.

Please return the completed, signed and notarized (or witnessed) questionnaire in the enclosed stamped addressed envelope. You should fill out and mail in this questionnaire no later than [insert day 30 days after contractor mailed questionnaire]. If you should misplace the envelope provided, please mail your questionnaire to [insert contractor's name and address].

APPENDIX C

ELIGIBILITY QUESTIONNAIRE

Please type or carefully print your answers.

Name *Address*

1. Did you enroll in the North American School of Conservation?
   ______ Yes ______ No
2. What was the *MOST IMPORTANT* reason why you enrolled? (MARK ONE BOX ONLY. Be sure to read all of the alternatives below before marking *the one* that applies to you.)

MARK ONLY ONE BOX

______ Primarily to increase my knowledge and further my education.
______ Primarily to enable me to get a job in the conservation or ecology field.
______ Primarily to get a promotion in my present job.
______ Primarily to help me decide if I wanted to go into the conservation or ecology field.
______ Primarily to enhance my enjoyment of the outdoors.
______ Other (please explain)

____

____

____

3. Generally speaking, were you satisfied with the course?

______ Yes
______ No
______ Somewhat satisfied, but not entirely.

4. If you *completed* the course, skip this question. If you did *not* complete the course, please give the *MOST IMPORTANT* reason why you did not complete the course. (MARK ONE BOX ONLY. Be sure to read all of the alternatives below before marking *the one* that applies to you.)

MARK ONLY ONE BOX

______ Primarily because I could no longer afford the course for financial reasons.
______ Primarily because I changed my career goal.
______ Primarily because I became convinced that the course would not help me get a job in the conservation or ecology field.
______ Primarily because I did not have enough time to study or I found the course materials too difficult.
______ Primarily because I was drafted or enlisted in the military service.

_____ Primarily because I went to college or other schooling.
_____ Primarily because I married, started a family, or stopped taking the course for other personal reasons such as illness or relocation.
_____ Other (please explain)
____
____
____

5. Did you try to get a job in the conservation or ecology field?
_____ Yes _____ No (If no, skip to question 8.)

6.(a) Please list as many agencies or employers that you can recall where you filled out or submitted a *written application* for employment in the conservation or ecology field and the approximate date of your application. (If you need more space, please use the back of this page or add more pages.)

Agency or Employer Approximate Date
____
____
____

(b) Please list as many agencies or employers that you can recall you *wrote to* about employment in the conservation or ecology field, but to which you did *not* make written application for a job. *Also,* please give the approximate date when you wrote, and a brief summary of the reply you received. (If you need more space, please use the back of this page or add more pages.)

Agency or Employer: ________________________
Approximate Date: ________________________
The reply I received was: ________________________
____
____

Agency or Employer: ________________________
Approximate Date: ________________________
The reply I received was: ________________________
____
____

Agency or Employer: ________________________
Approximate Date: ________________________
The reply I received was: ________________________
____
____

(c) Please list as many agencies or employers that you can recall you *personally visited* to see employment in the conservation or ecology field and the approximate date that you visited. *Also,* please identify the person you spoke with and give a brief summary of what happened. Tell what questions you asked and what you were told. (If you need more space, please use the back of this page or add more pages.)

Agency or Employer: ________________________
Approximate Date: ________________________
Name, title, position or description of person you spoke with:
____
____

The questions I asked and the answers I received were:
____
____
____

Agency or Employer: ______________________
Approximate Date: ______________________
Name, title, position or description of person you spoke with:
____
____
____
The questions I asked and the answers I received were:
____
____
____
Agency or Employer: ______________________
Approximate Date: ______________________
Name, title, position or description of person you spoke with:
____
____
The questions I asked and the answers I received were:
____
____
____

(d) Please list as many agencies or employers that you can recall you *telephoned* with regard to employment in the conservation or ecology field and the approximate date that you telephoned. *Also,* please give a brief summary of what happened. Tell what questions you asked and what you were told. (If you need more space, please use the back of this page or add more pages.)
Agency or Employer: ______________________
Approximate Date: ______________________
The questions I asked and the answers I received were:
____
____
____
Agency or Employer: ______________________
Approximate Date: ______________________
The questions I asked and the answers I received were:
____
____
____
Agency or Employer: ______________________
Approximate Date: ______________________
The questions I asked and the answers I received were:
____
____
____

(e) Did you contact North American School of Conservation for assistance in getting a job?
______ Yes ______ No
If yes, approximately when? ______________________

7. Did you get a job in the conservation or ecology field within 2 years of completing or dropping out of the course?
______ Yes ______ No

8.(a) Did any private business or other organization, or any government agency or department other than the Veterans Administration, pay any of the tuition for the course in which you enrolled? (Do not include any loan which you have repaid, are repaying, or are obligated to repay.)

_____ Yes _____ No

(b) If yes, how much of your tuition was paid by each private business, or organization, or government agency or department? (Do not include any loan which you have repaid, are repaying, or are obligated to repay.)

Amount $_______________

In order for you to be eligible for any tuition adjustment, you must, after completing the questionnaire, sign the following Affidavit in the presence of a Notary Public. However, if there is not a Notary Public within twenty-five (25) miles of the place you live, you may sign the Affirmation in the presence of three (3) witnesses who are not related to you and who are eighteen (18) years of age or older.

Also, in order for you to be eligible for any tuition adjustment, you must mail us the completed questionnaire promptly. Please mail the questionnaire by [insert date 30 days after contractor mailed questionnaire]. If you misplace the enclosed postage-prepaid envelope, you should mail the completed questionnaire to [insert contractor's name and address].

WARNING: It is a federal crime for anyone to knowingly and willfully make a false, fictitious, or fraudulent statement or representation in any matter within the jurisdiction of any department or agency of the United States. (18 U.S.C. 1001.)

AFFIDAVIT

I hereby affirm that I am the person to whom this questionnaire was sent and that I have answered the above questions completely and truthfully, to the best of my knowledge.

____

Signature

Subscribed and sworn to before me this _______________ day of _____ , _____ .

My commission expires: _____

Notary Public

If and only if you live more than 25 miles away from a Notary Public, you may sign this before 3 witnesses other than your spouse or relative; but all 3 witnesses must fill in the blanks below.

AFFIRMATION

I hereby affirm that I am the person to whom this questionnaire was sent and that I have answered the above questions completely and truthfully, to the best of my knowledge.

Signature

We affirm that we witnessed *(name of student)* sign the above statement; that we are not related to *(name of student)* by blood or marriage; that we are each at least eighteen (18) years of age; and that we hereby sign our names as attesting witnesses.

1. _______________

Signature

____

Address Date

2. ______________
Signature

Address ______________________ Date

3. ______________
Signature

Address ______________________ Date

APPENDIX D

(Name)
(Address)
Dear (Name):

Pursuant to an Order of the Federal Trade Commission, agreed to by this company, you are requested to provide us with the last known address of [insert name of student].

It is believed that this person was a student in the North American School of Conservation between 1973 and 1976. The Federal Trade Commission has determined that it is necessary to collect information from certain North American Conservation students to implement the terms of an Order which, among other things, requires the company to make tuition adjustments for certain students, possibly including the person named above.

If you know the current address of the person named above, please write it in the place provided at the bottom of this page and return it to us in the enclosed postage prepaid envelope as soon as possible, but *not later than* [insert date representing the one hundred and thirtieth (130th) day after the date of service].

Your cooperation will be appreciated.

Sincerely,

____
(current address of person listed above)
____

APPENDIX E

(Name)
(Address)
Dear (Name):

This letter relates to the questionnaire about your enrollment in the North American School of Conservation which you recently returned to us. We cannot evaluate your response because you marked more than one answer to Question[s] [2 and/or 4]. In order for us to evaluate your response you must return the enclosed copy of Question[s] [2 and/or 4] with ONLY ONE answer marked under [that, those] question[s]. You may not receive a tuition adjustment unless you mark ONLY ONE answer to [the, each] question.

Select the ONE answer for Question[s] [2 and/or 4] that best applies to you. You are reminded that your answer[s] must be truthful to the best of your knowledge.

Although your response to this inquiry need not be notarized or witnessed, you can be subjected to the same criminal penalties for an untruthful answer as you would be for untruthful answers to the Eligibility Questionnaire itself.

Your answer, on the enclosed copy of Question[s] [2 and/or 4] must be mailed to us not later than [insert date representing the earlier of the twenty-first (21st) day after contractor mails this letter or the one hundred and ninetieth (190th) day after the date of service]. If you misplace the enclosed postage-prepaid envelope, mail your answer[s] in an envelope addressed to [independent contractor's address].

By ______________

Enclosures

APPENDIX F

(Name)
(Address)
Dear (Name):

Pursuant to a Consent Order issued by the Federal Trade Commission, the North American School of Conservation has agreed to make a partial tuition adjustment for certain former students in its Conservation courses.

The Order of the Commission contains the provisions identifying the class of persons eligible for adjustments, and the procedures for making adjustments. (You may obtain a copy of the Order without charge by writing to the Federal Trade Commission, Public Reference Branch, Room 130, Washington, DC 20580. Refer to National Systems Corp., *et al.,* Docket No. 9078.)

In accordance with the provisions of the Order, it has been determined that you are entitled to a tuition adjustment of $______________ . A check for this amount is enclosed.

NORTH AMERICAN SCHOOL OF
CONSERVATION
By ______________

APPENDIX G

IMPORTANT NOTICE

Pursuant to an Order of the Federal Trade Commission issued on ______________ , the North American School of Conservation agreed to make a partial tuition adjustment for certain former students in its Conservation courses. The Order of the Commission contains provisions identifying the class of persons eligible for adjustments and the procedures for making adjustments.

In accordance with Part III of the Order, it has been determined, based upon your responses to the "Eligibility Questionnaire," that you are not eligible for an adjustment. A copy of this Order is enclosed.

NORTH AMERICAN SCHOOL OF
CONSERVATION
By ______________

APPENDIX H

INSTRUCTIONS TO INDEPENDENT CONTRACTOR

Respondent North American Correspondence Schools (NACS) shall require the independent contractor referred to in Part III of the Order to comply with the following instructions:

Determination of Eligible Class Members

The contractor shall receive the responses to the Appendix C Eligibility Questionnaire. From these responses, the contractor will determine all eligible class members, and, supplemented by NACS's records, the amount of refund to which each member is entitled, pursuant to the terms of Part III of this Order. All references regarding question numbers refer to the questions on the Appendix C Eligibility Questionnaire.

a. Vocational Intent Requirement

By checking the second response to question 2, the respondent to the questionnaire shall have met the requirement that she (he) enrolled in a NACS conservation course to enable her (him) to get a job in the conservation or ecology field. The contractor shall evaluate any answers to the sixth response to question 2 in Order to make a reasonable determination as to whether the respondent to the questionnaire met this requirement. If the respondent to the questionnaire checks two or more responses, one of which is a qualifying answer and one or more others is (are) disqualifying answer(s), and the respondent is not disqualified on the basis of an answer to any other question, then the contractor shall follow the procedure set forth in Paragraph III(6) of the Order. That is, within five (5) days after receiving the questionnaire, the contractor shall send, via first class mail, an envelope to the student bearing the contractor's return address and containing (a) a letter in the language, manner and form shown in Appendix E to the Order; (b) a copy, from an unanswered questionnaire, of that question or those questions to which the student had given inconsistent answers in her (his) first response; and (c) a first class postage-prepaid envelope addressed to the contractor.

b. Question 3

The contractor shall ignore the answers to question 3 in her (his) initial determination of eligibility.

c. Dropouts

Question 4 is to be answered only by those who did not complete NACS's conservation course. By checking the third response to question 4, the respondent to the questionnaire shall have met the requirement that the reason for not completing the course was that she (he) did not believe the course would help in getting employment in the conservation or ecology field. The contractor shall evaluate any answers to the eighth response to question 4 in order to make a reasonable determination as to whether the respondent to the questionnaire met this requirement. If the respondent to the questionnaire checks a qualifying answer and one or more disqualifying answer(s), but is not otherwise disqualified on the basis of an answer to any other question, then the contractor shall follow the procedure set forth in Paragraph III(6) of the Order. That is, within five (5) days after receiving the questionnaire, the contractor shall send, via first class mail to the student, an envelope bearing the contractor's return address and containing (a) a letter in the language, manner and form shown in Appendix E to the Order; (b) a copy, from an unanswered questionnaire, of that question or those questions to which the student had given inconsistent answers in her (his) first response; and (c) a first class postage-prepaid envelope addressed to the contractor.

d. Meaningful Attempts to Find a Job

Those who completed NACS's course in conservation must have made three meaningful attempts to find a job in conservation or ecology at least one of which was either a written application or a personal visit. Those who did not complete said course must have made two meaningful attempts. An attempt may be made in person, in writing, or by telephone. A "yes" answer to question 6(e) establishes the fact of one meaningful attempt. In determining whether any other action or effort constitutes a meaningful attempt, the contractor shall be governed by the criteria set forth in Paragraph III(9) of the Order. That is, a meaningful attempt is one in which the student:

(a) Filed a written application for employment with an agency or other employer in the conservation or ecology field, and can reasonably identify the agency or employer to which, and the approximate date on which, application was made;

(b) Wrote to an agency or employer in the conservation or ecology field to inquire about employment, and can reasonably identify the agency or employer to which, and the approximate date on which, the inquiry was sent;

(c) Contacted the North American School of Conservation for assistance in getting a job in the conservation or ecology field;

(d) Telephoned an employer in the conservation or ecology field to inquire about the availability of a conservation or ecology job but failed to apply for a conservation or ecology job because (1) she (he) was ineligible to apply, (2) she (he) chose not to apply because the salary was too low, or (3) she (he) was advised that no jobs were available; and can reasonably identify the agency or employer contacted and the approximate date of the contact; or

(e) Personally visited an employer in the conservation or ecology field to inquire about the availability of a conservation or ecology job but failed to apply for a conservation or ecology job because (1) she (he) was ineligible to apply, (2) she (he) chose not to apply because the salary was too low, or (3) she (he) was advised that no jobs were available; and can reasonably identify the agency or employer contacted, the person to whom she (he) spoke (name, position, title or description), and the approximate date of the contact.

A student who completed the course must have provided a total of at least three (3) acceptable responses under these criteria to questions 6(a) through 6(e) of the Eligibility Questionnaire, of which at least one (1) must have been an acceptable response under these criteria to question 6(a) or 6(c).

A student who did not complete the course must have made two (2) meaningful attempts to find a job; thus, such student must have provided a total of at least two (2) acceptable responses under these criteria to questions 6(a) through 6(e) of the questionnaire.

e. Obtained Employment

A student who obtained employment in the conservation or ecology field within two (2) years after completing, cancelling or being terminated from the course is not eligible for a tuition refund. Therefore, any student who answered "Yes" to question 7 shall be deemed ineligible.

f. Out of Pocket Payments for Tuition

In determining the amount of refund to which an eligible class member is entitled, the contractor shall be guided by the provisions of Paragraph III(13) of the Order. Where an eligible class member's tuition was paid by a private business or organization or by a state or federal agency (other than the Veterans Administration) in whole or in part, that member shall not receive an amount greater than the amount not paid for by such business, organization or agency. To determine the amount of such tuition assistance an eligible class member received, the contractor shall contact NACS for any records it may have indicating the nature and amount of such assistance. If NACS does not have such records, then the contractor may refer to the response to question 8 of the questionnaire in determining the amount to be paid to the eligible class members.

If NACS's records indicate that an eligible class member had not paid for all of the lessons completed prior to cancellation or termination of her (his) enrollment, the contractor shall deduct from the refund to which the student is otherwise entitled the pro rata cost for the lessons she (he) completed but for which she (he) had not paid. Thus, for example, if a student had enrolled in the one hundred (100) lesson course with a total tuition cost of five hundred dollars ($500.00), and had completed sixty (60) lessons (for which the pro rata cost would be $300.00), but paid only two hundred and fifty dollars ($250.00) in tuition, that student would have fifty dollars ($50.00) deducted from the refund to which she (he) would otherwise be entitled.

g. Affidavit and Affirmation Forms

If a questionnaire is not properly sworn or witnessed, the contractor shall photostat and promptly return the original questionnaire to the respondent of the questionnaire along with new Affidavit and Affirmation forms and the following notice:

> "We are returning your questionnaire because you did not properly sign it. Enclosed is a new Affidavit which you must sign before a notary public. *But* if you live more than twenty-five (25) miles from the nearest notary public, then sign the enclosed Affirmation before three witnesses (spouse and relatives don't count). Please sign the proper form and mail it along with the questionnaire within 2 weeks to *(name, and address)*. If you fail to do so, you will be ineligible for a tuition adjustment."

If respondent challenges the eligibility of a student initially determined to be eligible on the ground that the student signed before three witnessess rather than before a notary public notwithstanding the fact that the student lives within twenty-five (25) miles of a notary public, and respondent furnishes evidence that the student in fact lives within twenty-five (25) miles of a notary public, the contractor shall photostat and promptly return the original questionnaire to the student along with a new Affidavit and the following notice:

> "We are returning the questionnaire because you did not properly sign it. Since you live within twenty-five (25) miles of a notary public, you should have signed the Affidavit before a notary public rather than the Affirmation before three witnesses. Enclosed is a new Affidavit which you must sign before a notary public. Please sign it and mail it along with the questionnaire within 2 weeks to *(name and address)*. If you fail to do so, you will be ineligible for a tuition adjustment."

h. Resolution of Challenges

In resolving challenges to the contractor's initial determinations of eligibility, the contractor shall be governed by the provisions of Part III(11)(b) of the Order. That is, the contractor shall consider all evidence presented to it that bears on the appropriateness and reasonableness of the contractor's interpretation of responses to the questionnaire and all evidence presented to it that bears on the accuracy or veracity of a student's responses to the questionnaire. Such evidence may include, *inter alia,* (1) evidence that the student has answered a question on the questionnaire in a manner inconsistent with the student's answer or answers to a previous questionnaire or inquiry, (2) evidence that the student did not in fact file a written application or otherwise contact an agency or employer listed on the questionnaire, and (iii) the student's failure to have the questionnaire notarized or affirmed in compliance with the questionnaire's instructions. The contractor's decision in upholding or denying any challenge shall be fair and impartial. No financial or other material benefit shall accrue to the contractor contingent upon the nature of the outcome of her (his) decision.

IN THE MATTER OF

ZAYRE CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2951. Complaint, Jan. 19, 1979 — Decision, Jan. 19, 1979

This consent order, among other things, requires a Framingham, Mass. discount department store chain to cease inducing or receiving discriminatory promotional allowances, services or facilities from its suppliers; and prohibits the firm from boycotting or decreasing its purchases from recalcitrant suppliers. The company is also required to maintain specified records for a five-year period; and to bear all costs of any trade show it sponsors, organizes or directs.

Appearances

For the Commission: *David W. DiNardi* and *Norman H. Jackman.*

For the respondent: *Harry L. Shniderman, Covington & Burling,* Washington, D.C.

COMPLAINT

The Federal Trade Commission, having reason to believe that Zayre Corp., a corporation, has violated the provisions of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), and believing that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating its charges with respect thereto as follows.

I. Respondent

PARAGRAPH 1. Respondent Zayre Corp. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its office and principal place of business located at 770 Cochituate Road, Framingham, Massachusetts.

PAR. 2. Respondent is now and for many years has been engaged in the business of selling general merchandise to the public at retail. Respondent operates a chain of discount department stores which sell a large variety of clothing, hard goods, and other general merchandise. There are presently approximately two hundred and sixty department stores in respondent's chain, which stores are located in twenty-six states in the eastern half of the United States. Its sales in fiscal 1977 amounted to $1,160,572,000.

PAR. 3. In the course and conduct of its business, respondent is now and has been in competition with other corporations, persons, firms, and partnerships in the purchase, sale, and distribution of clothing, hard goods, and general merchandise, except to the extent limited or restrained by the practices identified hereinafter.

II. Commerce

PAR. 4. In the course and conduct of its business, respondent has been and is now engaged in activities which are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, in the following manner:

(a) Respondent purchases for resale a great variety of general merchandise from a large number of suppliers located throughout the United States. Respondent causes these products to be transported from the places of manufacture or purchase to its stores or warehouses located in various states throughout the eastern half of the United States for resale to the general public. In many instances, respondent causes merchandise delivered to its warehouses to be transported to its stores located in other states.

(b) In addition, respondent disseminates advertising in commerce and receives payments in commerce from suppliers for advertising and promotional services and facilities, including those described hereinafter.

III. Inducing Discriminatory Allowances

PAR. 5. In the course and conduct of its business in or affecting commerce, respondent has knowingly induced and received, or received, from some of its suppliers, the payment of something of value to respondent or for respondent's benefit, as compensation for or in consideration of services or facilities furnished by or through respondent in connection with respondent's offering for sale, or sale, of products sold to respondent by the aforesaid suppliers. In particular:

(a) In July of 1972, respondent held a trade show in Miami Beach, Florida, at which products of its suppliers were displayed. This trade show was organized, directed, and conducted by respondent and was attended by respondent's officials and employees, as well as by a substantial number of respondent's suppliers. The show was not open to the public.

(b) Respondent solicited many of its suppliers to participate in said trade show and induced from each such participating supplier payment for the rental of booth space at said trade show. The amount of such money induced and received, or received, by respondent from participating suppliers was substantial. Approximately 190 suppliers paid $700,000 in financial payments, allowances and other things of value to proposed respondent.

(c) In the course and conduct of said trade show, respondent required each participating supplier to provide valuable services, including staffing the booths rented by said suppliers from respondent and demonstrating and promoting the products displayed therein. In addition to the furnishing of such services, other services were performed by suppliers which aided said respondent in the resale of suppliers' products. The value of such services induced and received, or received, by respondent was substantial.

(d) Respondent threatened to eliminate or boycott or decrease purchases from, or has eliminated or boycotted or decreased purchases from, suppliers which refused to participate in said trade show.

PAR. 6. Some of respondent's suppliers who participated in the aforesaid trade show did not offer or otherwise make available to all their customers competing with respondent in the sale and distribution of their respective products payments, allowances, services, or other things of value, for advertising and promoting such products, on proportionally equal terms to those granted respondent in connection with its trade show.

PAR. 7. Furthermore, respondent has also knowingly solicited and induced from a major supplier, discriminatory payments for services in connection with the resale of certain products in the regular course of its business during the years 1972, 1973, and 1974. Respondent has received substantial sums from this supplier for each of the years 1972, 1973, and 1974.

PAR. 8. When respondent induced and received, or received, such payments, allowances, services, facilities, or other things of value from suppliers, said respondent knew or should have known that it was inducing and receiving, or receiving, payments, allowances, services, facilities, or other things of value from suppliers, which said suppliers were not offering or otherwise making available on proportionally equal terms to all of the suppliers' other customers who were competing with respondent in the sale and distribution of their respective products.

PAR. 9. The methods, acts, and practices of respondent, as herein alleged, are all to the prejudice of the public and constitute unfair methods of competition in or affecting commerce and unfair acts and practices in or affecting commerce within the intent and meaning of and in violation of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Boston Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Zayre Corp. is a corporation, organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its offices and principal place of business located at 770 Cochituate Road, Framingham, Massachusetts.
2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

I

It is ordered, That Zayre Corp., a corporation, its successors and assigns, and its officers, and respondent's agents, representatives, and employees, directly or through any corporation, subsidiary, division, or other device in connection with the purchase in or affecting commerce, or receipt of merchandise on consignment in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, of products for resale by the respondent, or in connection with any other transaction between respondent and its various suppliers involving or pertaining to the regular business of the respondent in purchasing, promoting, advertising, distributing, and/or selling: books, phonograph records, photo finishing, photo film, photo equipment, franchise cosmetics, candy, health and beauty aids, home and office stationery, greeting cards, gift wrap, paper goods, party goods, and candles in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

1. Inducing and receiving, receiving, or contracting for the receipt of, any promotional allowance, payment, or other thing of value, solicited by respondent from any supplier, including any consignor or vendor, as compensation for or in consideration of any advertising or promotional service, furnished by or through respondent in connection with promotions originating with or sponsored by respondent, and involving the respondent's sale or offering for sale of the above-listed products, when respondent knows or should know that such compensation is not affirmatively offered or otherwise made available by such supplier, including any consignor or vendor, on proportionally equal terms to all of its customers competing with respondent, including any customer who purchases from any intermediary and competes with respondent in the resale of any such product of any such supplier.

2. Inducing and receiving, receiving, or contracting for the receipt of, the furnishing of any service or facility solicited by respondent from any supplier, including any consignor or vendor, in connection with promotions originating with or sponsored by respondent, and involving respondent's sale or offering for sale of the above-listed products, when respondent knows or should know that such service or facility is not affirmatively offered or otherwise made available by such supplier, including any consignor or vendor, on proportionally equal terms to all of its customers competing with respondent, including any customer who purchases from any intermediary and competes with respondent in the resale of any such product of any such supplier.

3. Eliminating or boycotting or decreasing purchases from any supplier or suppliers because of such suppliers' refusal to grant any allowance or payment in connection with the processing, handling, sale, or offering for sale of the above-listed products, or refusal to furnish any service or facility connected with respondent's sale or

offering for sale of any such product, when respondent knows or should know that such allowance, payment, service, or facility is not affirmatively offered or otherwise made available by such supplier, including any consignor or vendor, on proportionally equal terms to all of its customers competing with respondent, including any customer who purchases from an intermediary and competes with respondent in the resale of any such product of any such supplier.

II

It is further ordered, That respondent shall not organize, direct, or sponsor any trade show unless respondent bears the full cost of the operating expense of any such trade show.

III

It is further ordered, That, for a period of five (5) years from the date of service upon it of this order, respondent shall establish and maintain at its General Office in Framingham, Massachusetts, a separate file containing each offered promotional allowance, payment, or other thing of value, induced and received within the meaning of Paragraph I of this order. The file shall be maintained alphabetically, according to suppliers with all offers and related materials pertaining to each supplier filed chronologically, within that supplier's portion of the file. The information shall be maintained for the effective period of this order. The file shall be made available to employees of the Federal Trade Commission, for inspection and copying, upon written notice of ten (10) calendar days.

IV

It is further ordered, That respondent, within thirty (30) days after the date of service upon it of this order, shall distribute a copy of this order to each of its officers and managers of each of its divisions and subsidiaries.

V

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent, such as dissolution, assignment, or sale, resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation that may affect compliance obligations arising out of this order.

VI

It is further ordered, That the respondent herein shall, within sixty (60) days after service upon it of this order file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

IN THE MATTER OF

THE AMERICAN SOCIETY OF ANESTHESIOLOGISTS, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2952. Complaint, Jan. 22, 1979 — Decision, Jan. 22, 1979

This consent order, among other things, requires a Park Ridge, Ill. medical society, composed mainly of physicians who have limited their professional activities to the practice of anesthesiology, to cease including statements relating to compensation arrangements in membership documents; conditioning membership privileges on such arrangements; or engaging in any act or practice which would serve to influence the prices members charge for their services. The Society is further required to delete from its files any record of disciplinary sanctions imposed upon members for failure to adhere to past pricing policies, and advise affected parties of such deletion. Additionally, the Society would be required to revoke the charter of any component society which fails to comply with the terms of the order.

Appearances

For the Commission: *M. Elizabeth Gee* and *James E. McCarty.*
For the respondent: *Squire, Sanders & Dempsey,* Washington, D. C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, 15 U.S.C. 41, *et. seq.,* and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that The American Society of Anesthesiologists, Inc. has violated the provisions of Section 5 of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

PARAGRAPH 1. Respondent, The American Society of Anesthesiologists, Inc. ("ASA"), is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its principal office and place of business located at 515 Busse Highway, Park Ridge, Illinois.

PAR. 2. ASA has approximately 15,000 members, which amounts to approximately 90 percent of all anesthesiologists practicing in the United States. Its members are comprised mainly of those physicians who have completed post-graduate training in, and who have limited their professional activities to, the practice of anesthesiology or are otherwise especially interested in anesthesiology. The members elect the officers of ASA, who, together with the Board of Directors, manage the affairs of ASA.

PAR. 3. Anesthesiologists are licensed physicians who specialize in rendering a patient insensitive to pain. They are generally engaged in the private practice of medicine and derive substantial portions of their professional income from fees for medical treatment charged to patients or to insurers.

PAR. 4. ASA has engaged in activities relating to the economic aspects of the practice of anesthesiology, including the development and distribution of relative value guides and the promulgation of the *Guidelines to the Ethical Practice of Anesthesiology* and *Statement of Policy* which relate in part to the financial aspects of anesthesia practice, as a result of which ASA is organized for the profit of its members within the meaning of Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

PAR. 5. In the course and conduct of their business, the members of ASA:

(a) charge and collect fees which, in substantial part, are paid or reimbursed to patients directly or indirectly with Federal funds through Medicare, Federal Employees Health Benefits Program, Civilian Health and Medical Program of the Uniformed Services, and other federal programs;

(b) charge and collect fees which, in substantial part, are paid or reimbursed to patients directly or indirectly by Blue Shield Plans and by commercial insurance carriers pursuant to group contracts covering insureds in two or more states; and

(c) practice anesthesiology and charge and collect fees therefor in the District of Columbia;

as a result of which the acts and practices of ASA and its members are in and affect commerce within the meaning of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

PAR. 6. Since at least 1968, ASA, individually and in collusion with its component societies and members, promulgated, published, approved and enforced documents entitled *Guidelines to the Ethical Practice of Anesthesiology* and *Statement of Policy.* Said documents include provisions which provide that anesthesiologists should be compensated only on a fee-for-service basis and that ASA members should not practice as salaried employees of organizations such as hospitals.

PAR. 7. The acts, practices and methods of competition alleged in Paragraph Six above have had the effect of:

(a) fixing, establishing, maintaining or otherwise influencing the prices which anesthesiologists charge for their services;
(b) limiting the ability of hospitals to freely negotiate and conclude contracts with ASA members and others;
(c) otherwise restraining, limiting, and foreclosing competition among anesthesiologists; and
(d) depriving consumers of the benefits of competition;

and are in violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days; and

Counsel for the Commission having thereafter submitted a revised order, and respondent and its counsel having submitted letters of agreement dated December 28, 1978, and January 8, 1979, assenting to the terms of the order, as modified; and

The Commission having duly considered the recommendations of its staff and the assent of respondent to the revised order, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order, as modified:

1. Respondent, The American Society of Anesthesiologists, Inc., is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located at 515 Busse Highway, in the City of Park Ridge, State of Illinois.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

I

For purposes of this order, the following definitions shall apply:

A. The term "ASA" means The American Society of Anesthesiologists, Inc., its successors or assigns, its committees or organizational subdivisions, and, in their capacities as such or while representing the Society, its officers, agents, representatives, employees or authorized delegates;

B. The term "Membership Document" means any document the acceptance of which or adherence to the terms of which is a condition of membership privileges;

C. The term "Official Position" means an oral or written statement which is made by ASA or any of its Component Societies;

D. The term "Component Society" means any organization duly chartered as such by ASA, any successor or assign to any Component Society, any committee or organizational subdivision of any Component Society, and, in their capacities as such or while representing a Component Society, any officers, agents, representatives, employees or authorized delegates; and

E. The term "Effective Date of This Order" means the date of service of this order.

II

It is ordered, That ASA directly or through any corporation, subsidiary, division or other device, or through employment of any method, act, practice or procedure, shall cease and desist from:

A. Importuning or engaging in threats or acts of reprisal, coercion, or intimidation with the purpose or effect of restraining or impeding anesthesiologists individually or as a class of practitioners from engaging in the practice of anesthesiology other than on a fee-for-service arrangement;

B. Including within any Membership Document any statement which relates to the fee-for-service, salary or any other compensation arrangement of anesthesiologists individually or as a class of practitioners; and

C. Conditioning any privilege of membership upon the fee-for-service, salary or any other compensation arrangement of anesthesiologists individually or as a class of practitioners.

III

It is further ordered, That, except as required by subpoena or other legal process, ASA is prohibited from publishing, disseminating or distributing in any manner any list, compilation, document or statement that refers to censure or other sanction against any present or former member, the grounds for which was failure of such member to accept or to adhere to the terms of any Membership Document or Official Position which prohibited anesthesiologists individually or as a class of practitioners from engaging in the practice of anesthesiology on other than a fee-for-service arrangement, and ASA shall advise any such members (if living) of this prohibition.

IV

It is further ordered, That ASA shall for a period of ten (10) years following the Effective Date of This Order cease and desist from making any statement which contains an Official Position which relates to the fee-for-service, salary or other compensation arrangement of anesthesiologists individually or as a class of practitioners, unless such statement contains and is not inconsistent with the following language:

> It is the official policy of The American Society of Anesthesiologists, Inc. that an anesthesiologist is free to choose whatever arrangement he prefers for compensation of his professional services. The Society does not consider the compensation arrangement so chosen to be a matter of professional ethics.

This part does not modify the requirements of Part II of this order.

V

It is further ordered, That ASA shall:

A. At the first Annual Meeting of ASA's House of Delegates subsequent to 180 days after the Effective Date of This Order, revoke the charter of any Component Society which, prior to the meeting of ASA's Board of Directors immediately preceding such Annual Meeting, has not informed ASA by a sworn statement of an authorized officer that the Component Society has (1) agreed to comply with the requirements of Part II of this order, and brought its own Membership Documents and Official Positions into conformity with the requirements of that part, (2) agreed to the prohibition of Part III of this order, so that, except as required by subpoena or other legal process, the Component Society is prohibited from publishing, disseminating or distributing in any manner, any list, compilation, document or statement that refers to censure or other sanction against any present or former Component Society or ASA member, the ground for which was failure of such member to accept or to adhere to the terms of any Membership Document or Official Position which prohibited anesthesiologists individually or as a class of practitioners from engaging in the practice of anesthesiology on other than a fee-for-service arrangement, and (3) agreed to abide by the requirements of Part IV of this order, so that every statement of the Component Society which contains an Official Position which relates to the fee-for-service, salary or other compensation arrangement of anesthesiologists individually or as a class of practitioners, contains and is not inconsistent with the following language:

> It is the official policy of [name of Component Society] that an anesthesiologist is free to choose whatever arrangement he prefers for compensation of his professional services. The [name of Component Society] does not consider the arrangement so chosen to be a matter of professional ethics.

B. Within 60 days after the Effective Date of This Order, distribute by first class mail a copy of the Commission's complaint and order in this matter to each of the aforesaid Component Societies and to each of ASA's then current members, together with a letter on ASA's regular letterhead in the form shown in the Appendix attached hereto.

VI

It is further ordered, That nothing in this order shall prohibit or limit the organizations and persons subject to this order from petitioning the government for a redress of grievances by:

A. Preparing or furnishing testimony, information or advice to, or negotiating with, any government body or agency or furnishing drafts thereof to any organization which is preparing or furnishing testimony, information or advice to, or negotiating with, any government body or agency with respect to the same subject matter;

B. Advising its members and others of legislation, programs, policies, regulations, procedures or interpretations of any government body or agency and soliciting their views thereon;

C. Informing members and others of any testimony, information or advice supplied to, or negotiations with, any government body or agency; and

D. Suggesting or recommending that members or others undertake the activities enumerated in subparagraphs (A), (B) and (C) above; but only as long as the activities enumerated in this Part VI are not undertaken with the purpose or intent of achieving a result prohibited by Part II of this order through means other than the action of a government body or agency.

VII

It is further ordered, That ASA shall, within sixty (60) days following the Effective Date of This Order, and thereafter on the first anniversary date of the Effective Date of This Order, and at such other times as the Commission may by written notice to the respondent require, file or cause to be filed with the Commission a report in writing, setting forth in detail the manner and form in which it has complied with this order. All compliance reports shall include such other information and documentation as may be required to show compliance with this order.

VIII

It is further ordered, That ASA shall notify the Commission at least thirty (30) days prior to any proposed change in its structure resulting in the emergence of a successor corporation, or any other change in its structure, which may affect obligations arising out of this order.

APPENDIX

[ASA REGULAR LETTERHEAD]

To the Members and Component Societies of the American Society of Anesthesiologists, Inc.:

As some of you have been aware, the Federal Trade Commission ("FTC") in September 1977 initiated an investigation of the extent to which members and component societies of ASA were required to accept or adhere to certain principles, contained in documents approved by the ASA House of Delegates, which related to the fee-for-service, salary or other compensation arrangements of anesthesiologists.

The Board of Directors and House of Delegates have determined that they do not desire to impose any such condition nor to impose any sanction against an ASA member for failure to accept or adhere to such principles. Accordingly, ASA has with approval of its House of Delegates reached agreement with the FTC, resulting in the issuance by the FTC of a complaint on ————, and the entry of a consent order.

294-972 O - 80 - 8

The complaint and the order are attached to this letter. The order, rather than this letter, is the document which legally binds ASA and others. You should carefully review it.

The complaint alleges that the promulgation and enforcement of those provisions of the Statement of Policy and Guidelines to the Ethical Practice of Anesthesiology which relate to compensation arrangements have had the effect of:

(a) fixing, establishing, maintaining or otherwise influencing the prices which anesthesiologists charge for their services;
(b) limiting the ability of hospitals to freely negotiate and conclude contracts with ASA members and others;
(c) otherwise restraining, limiting and foreclosing competition among anesthesiologists; and
(d) depriving consumers of the benefits of competition.

The agreement containing the consent order states that it is for settlement purposes only and does not constitute an admission by ASA of the charges in the complaint or that the law has been violated. The consent order itself requires, in summary, that ASA:

(a) Refrain from importuning or engaging in threats or acts of reprisal, coercion, or intimidation with the purpose or effect of restraining or impeding anesthesiologists individually or as a class of practitioners from engaging in the practice of anesthesiology other than on a fee-for-service arrangement;
(b) Not include within any membership document any statement which relates to the fee-for-service, salary or any other compensation arrangement of anesthesiologists;
(c) Not condition any privilege of membership upon the fee-for-service, salary or any other compensation arrangement of anesthesiologists;
(d) Not publish, disseminate or distribute (unless required to do so by subpoena or other legal process) any list, compilation, document or statement that refers to censure or other sanction imposed upon any member for failure to accept or adhere to any position or policy which prohibited anesthesiologists from practicing on other than a fee-for-service arrangement, and notify any such member of this prohibition;
(e) For a period of ten years, refrain from making any statement which contains an ASA official position which relates to the fee-for-service, salary or other compensation arrangement of anesthesiologists unless the statement contains and is not inconsistent with the following language:

> It is the official policy of The American Society of Anesthesiologists, Inc. that an anesthesiologist is free to choose whatever arrangement he prefers for compensation of his professional services. The Society does not consider the compensation arrangement so chosen to be a matter of professional ethics;

and

(f) Revoke the charter of any component society which does not (1) agree to abide by the provisions of the order, and (2) bring its own membership documents, guidelines, policies and statements into conformity with these provisions.

The order also provides that nothing in it shall prohibit or limit the organizations and persons subject to the order from petitioning the government for a redress of grievances by:

(a) Preparing or furnishing testimony, information or advice to, or negotiating with, any government body or agency or furnishing drafts thereof to any organization which is preparing or furnishing testimony, information or advice to, or negotiating with, any government body or agency with respect to the same subject matter;

(b) Advising its members and others of legislation, programs, policies, regulations, procedures or interpretations of any government body or agency and soliciting their views thereon;

(c) Informing members and others of any testimony, information or advice supplied to, or negotiations with, any government body or agency; and

(d) Suggesting or recommending that members or others undertake the activities enumerated in subparagraphs (a), (b) and (c) above;

but only as long as the activities enumerated above are not undertaken with the purpose or intent of achieving a result which is prohibited by the order through means other than the action of a government body or agency.

Henceforth, it will be the official policy of ASA that an anesthesiologist is free to choose whatever method he prefers for compensation of his professional services, and that the compensation arrangement so chosen will not be a matter of professional ethics. The financial arrangements between an anesthesiologist and a hospital or other institutional provider of health care will not be the basis for the denial to an anesthesiologist of ASA membership or any privilege of ASA membership.

Sincerely,

IN THE MATTER OF

COCA-COLA BOTTLING COMPANY OF NEW YORK, INC.

DISMISSAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND CLAYTON ACTS

Docket 8992. Complaint, Sept. 10, 1974 — Final Order, Jan. 23, 1979

This order dismisses a complaint issued against a New York City producer and marketer of various products, including soft drinks and wine, for alleged violations of Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act. The Commission, in dismissing the complaint, held that evidence failed to establish that the firm's merger with Franzia Bros. Winery would substantially lessen competition.

Appearances

For the Commission: *Joseph S. Brownman, John F. Stephens, Jr., Charles G. Brown* and *Elizabeth M. Brown.*

For the respondent: *Christopher Crowley, Arthur F. Golden, Michael Mills* and *Susan K. Jackson, Davis, Polk & Wardwell,* New York City.

COMPLAINT

The Federal Trade Commission having reason to believe that Coca-Cola Bottling Company of New York, Inc. (hereafter New York Coca-Cola), a corporation and the respondent herein, has violated the provisions of Section 7 of the amended Clayton Act (15 U.S.C. 18) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45) by its acquisition of Franzia Brothers Winery (hereafter Franzia), hereby issues this complaint stating its charges as follows.

I. ACQUIRING COMPANY

PARAGRAPH 1. Respondent New York Coca-Cola is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 425 East 34th St., New York, New York.

PAR. 2. New York Coca-Cola is a major industrial corporation engaged in three lines of business: (i) the production and sale of soft drinks, (ii) the production and sale of wines, and (iii) the manufacture and marketing of picnic chests, beverage coolers and extruded plastic sheet. New York Coca-Cola sales doubled during the last five years. Net sales for its fiscal years ending December 31 were:

$211,584,000 in 1972; $189,698,000 in 1971; $141,549,000 in 1970; $117,730,000 in 1969; and $103,421,000 in 1968.

PAR. 3. New York Coca-Cola is engaged primarily in the production and marketing of Coca-Cola, Fresca, Tab, Sprite and Fanta flavors in bottles, cans and bulk containers. In 1970 and 1971 New York Coca-Cola further expanded its line of soft drinks when it obtained franchises from Dr. Pepper Company to produce and market bottled and canned Dr. Pepper [2] and Sugar Free Dr. Pepper. In 1972 New York Coca-Cola acquired the Igloo Corporation which manufactures and markets on a national basis picnic chests, beverage coolers and extruded thermoplastic sheet.

PAR. 4. New York Coca-Cola entered the wine industry with its acquisition of Mogen David Wine Corporation (hereafter Mogen David) in 1970. Recently, New York Coca-Cola expanded its wine business with the acquisition of Tribuno Wines, Inc. (hereafter Tribuno) in 1973. With these acquisitions New York Coca-Cola became one of the leading producers of wine in the United States. The wine products of both of these wholly-owned subsidiaries are marketed throughout the United States. The Franzia acquisition represents the third such acquisition in the wine industry by New York Coca-Cola.

PAR. 5. New York Coca-Cola is the fifth largest producer of wine in the country. In 1972 Mogen David and Tribuno accounted for 3.9 percent of wine sales in the United States and 4.6 percent of the sales of domestically produced wine in the United States. 1972 was an excellent year for Mogen David. The company enjoyed a sales growth of 32 percent, far outstripping the wine industry's 10 percent average growth. Mogen David has begun marketing three new products, Cold Bear, Mogen David Concord, and MD 20 20, each of which have sold over one million cases in their second year of distribution. This represents a sales level attained by only a handful of brands in the American wine industry.

PAR. 6. As a result of its Tribuno acquisition, New York Coca-Cola is the largest producer of vermouth in the United States. Tribuno holds a 12.3 percent share of the total vermouth market, and its share of domestically produced vermouth is 24 percent. Thus, Tribuno ranks first among all domestic sellers of vermouth and second among all producers of vermouth.

PAR. 7. Advertising in various media is relied upon extensively by New York Coca-Cola in the marketing of soft drinks, wine, picnic chests and beverage coolers. New York Coca-Cola has the third largest advertising budget in the wine industry.

PAR. 8. In 1972 Mogen David wines and Tribuno vermouths were marketed nationally through over 300 independent distributors. In addition Mogen David has a staff of over 45 salesmen. New York Coca-Cola has begun to consolidate Tribuno with Mogen David distribution in order to strengthen its market position. [3]

PAR. 9. At all times relevant herein, New York Coca-Cola sold and shipped its products in interstate commerce and engaged in "commerce" within the meaning of Section 7 of the amended Clayton Act and Section 5 of the Federal Trade Commission Act.

II. ACQUIRED COMPANY

PAR. 10. Franzia is a corporation organized and existing under the laws of the State of California, with its principal place of business located at 1700 East Highway 120, Ripon, California.

PAR. 11. Franzia is now and for many years has been engaged in the production, distribution and sale of wines of all types including table wines, sparkling wines, dessert wines and vermouth.

PAR. 12. Franzia is one of the principal producers of generic table wines in the United States. Ranking eighth among all wine producers in 1972, Franzia accounted for approximately 3 percent of wine products produced and sold in the United States and 2.4 percent of all wine products sold in the United States. Franzia has been experiencing a strong growth trend with dollar sales increasing from approximately $8 million in 1968 to approximately $29 million for its fiscal year ending July 31, 1973. Franzia's assets exceed $20 million. In its fiscal year ending July 31, 1973, Franzia's sales in gallons and dollars increased 32 percent and 38 percent, respectively, over the previous year. The rate of growth for Franzia for the past three years was substantially greater than that recorded by the wine industry as a whole. Franzia has relied primarily on price competition in expanding its sales, maintaining a low level of advertising expenditures.

PAR. 13. Franzia distributes its wine directly to retail outlets in California and through independent distributors in 40 other states and the District of Columbia. In addition to Franzia's own products, Franzia distributes wine products for Gibson Wine Company, Charles Krug and Robert Mondavi.

PAR. 14. At all times relevant herein Franzia sold and shipped its products in interstate commerce and engaged in "commerce" within the meaning of Section 7 of the amended Clayton Act and Section 5 of the Federal Trade Commission Act. [4]

III. Acquisition

Par. 15. On December 14, 1973, New York Coca-Cola finalized its acquisition of Franzia. The transaction was cast as an acquisition of the assets of Franzia by a New York Coca-Cola subsidiary in exchange for common stock of New York Coca-Cola in such manner as to qualify as a tax-free reorganization.

IV. Trade and Commerce

Par. 16. The United States wine industry is in the midst of a period of exceptional growth as reflected by a dramatic increase in sales and consumption. Between 1967 and 1972 sales of wine products have increased from approximately 203 million gallons to 337 million gallons, representing an increase of more than 65 percent. During that period per capita consumption has increased from 1.0 gallons to 1.6 gallons, representing an increase of approximately 60 percent. According to reliable forecasts an estimated 650 million gallons will be distributed in 1980.

Par. 17. Unlike sales of other sweet wines (over 14 percent alcohol) which have declined, sales of vermouths have increased.

Par. 18. The wine industry is marked by increasing concentration. E & J Gallo Winery and United Vintners are the two largest wineries in the U.S. The largest four firms accounted for approximately 55 percent of all wine products sold in the United States in 1972. This represents an increase of 7 percent over the 1968 four firm concentration ratio of 48 percent The ten largest wineries accounted for approximately 70 percent of the wine sold in the United States. The remainder is shared among over 300 wineries.

Par. 19. Over the past ten years there has been a noticeable trend toward mergers and acquisitions involving wine producers.

Par. 20. There are major barriers to entry to any firm wishing to make a significant entrance into the wine business. The high cost of advertising presents a barrier to any winery wishing to sell on a national or even regional basis. Consumer appeal, created by advertising, is an important element in the marketing of wine products. Obtaining the services of independent wholesale distributors continues to be an important requirement for the successful marketing of wine products on a national, regional, and state level. The number of such distributors is closely regulated by state laws. [5]

V. Effect of Merger

Par. 21. The effect of the acquisition of Franzia by New York Coca-

Cola may be substantially to lessen competition or to tend to create a monopoly in the production, distribution and/or sale of wine products in the United States, in violation of Section 7 of the Clayton Act, as amended, and Section 5 of the Federal Trade Commission Act, 15 U.S.C. 18, 45, in the following ways, among others:

a. Substantial actual and potential competition between Franzia and New York Coca-Cola will be eliminated, prevented or lessened;

b. Franzia will be eliminated as a substantial independent factor in the production, distribution and sale of wine;

c. Independent distributors and sales representatives of Franzia products have been or may be, and potential independent distributors and sales representatives may be foreclosed from a high volume, fast moving account.

d. Concentration in the wine industry will be increased to the detriment of actual as well as potential competition;

e. An acceleration of the trend toward mergers and acquisitions will be encouraged and may contribute to further increases in concentration in the wine industry;

f. Barriers to entry into the production, distribution and sale of wine will be increased;

g. Franzia will no longer be able to adhere to its policy of price competition to expand sales and prices will be increased. [6]

PAR. 22. The merger of Franzia into New York Coca-Cola, in Paragraph 15, constitutes a violation of Section 7 of the Clayton Act, as amended, and an unfair method of competition and an unfair act and practice in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. 18, 45.

INITIAL DECISION BY LEWIS F. PARKER, ADMINISTRATIVE LAW JUDGE

JUNE 26, 1978

I. HISTORY OF THE PROCEEDING

The Commission issued its complaint in this case on September 10, 1974. The complaint challenges the acquisition of Franzia Brothers Winery ("Franzia") by the Coca-Cola Bottling Company of New York ("Coke-New York") as a violation of Section 7 of the Clayton Act, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45.

The complaint alleges that Franzia is one of the principal producers of generic table wines in the United States, and that its acquisition by Coke-New York, which had previously acquired two other wine producers, Mogen [2] David Wine Corporation ("Mogen David") and Tribuno Wines Inc. ("Tribuno"), may substantially lessen competition or tend to create a monopoly in the production, distribution and/or sale of wine products in the United States. The alleged effects of the acquisition are that:

a. Substantial actual and potential competition between Franzia and Coke-New York will be eliminated, prevented or lessened;

b. Franzia will be eliminated as a substantial independent factor in the production, distribution and sale of wine;

c. Independent distributors and sales representatives of Franzia products have been or may be, and potential independent distributors and sales representatives may be foreclosed from a high volume, fast moving account.

d. Concentration in the wine industry will be increased to the detriment of actual as well as potential competition;

e. An acceleration of the trend toward mergers and acquisitions will be encouraged and may contribute to further increases in concentration in the wine industry;

f. Barriers to entry into the production, distribution and sale of wine will be increased;

g. Franzia will no longer be able to adhere to its policy of price competition to expand sales and prices will be increased.

Coke-New York denied that its acquisition of Franzia would have the alleged effects. Several prehearing conferences were held in this case and the parties engaged in extensive discovery, including the issuance of subpoenas to many wine producers. The parties filed exhibit and witness lists and submitted trial briefs. [3]

Complaint counsel's case began on November 7, 1977 and concluded on December 16, 1977. Coke-New York's defense began on January 16, 1978 and concluded on January 27, 1978. Complaint counsel presented rebuttal evidence on February 27, 1978.

Complaint counsel called the following witnesses:

John W. Anderson	Sonoma Vineyards President
Robert H. Arnold	California Wine Association Vice President-Marketing
Saul Ben-Zeev	Creative Research Associates President
J. Kenneth Borders	Franzia Brothers Winery Former National Sales Coordinator

Arthur A. Ciocca	Franzia Brothers Winery President
Frederick DePompei	Pompei Winery, Inc. President
Angelo Fantozzi	Fantozzi & Trucco Company, Inc., Owner
John G. Franzia, Jr.	Bronco Wine Company Vice President-Production
Joseph S. Franzia	Bronco Wine Company Vice President-Sales
Ernest C. Haas	East-Side Winery General Manager
Robert Ivie	Guild Wineries and Distilleries, President
Marvin B. Jones	Gibson Wine Company General Manager
David Painter	Federal Trade Commission Staff Accountant
[4]Mario Perelli-Minetti	California Wine Association Vice President-Marketing
Meyer H. Robinson	Monarch Wine Company Secretary-Treasurer and General Manager
Marvin Sands	Canandaigua Wine Company President
Robert Setrakian	California Growers Winery, Inc., President
John E. Simon	Bardenheier's Wine Cellars Director of Marketing
William J. Sullivan	The Coca-Cola Bottling Company of New York, Inc. Executive Vice President
Fred E. Weibel	Weibel, Inc. President

Coke-New York called the following witnesses:

Michael A. Bernstein	Mt. Veeder Winery & Vineyards, Owner and General Manager

Harold Binstein	Gold Standards Liquors President
Michael T. Gelven	Big D Liquors Owner
Louis P. Martini	Louis M. Martini, Inc. President
Edmund A. Mirassou	Mirassou Vineyards Co-Owner
John Pearson	C & C Distributing Company Owner
Gary P. Raden	G. Raden & Sons Owner
Jack Robinson	Argonaut Liquors Co-Owner
[5]August Sebastiani	Sebastiani Vineyards President
Terry C. Whitney	Franzia Brothers Winery Former President

The record was closed on March 20, 1978 and the parties, who were given a two-week extension of time to do so, filed their proposed findings of fact and conclusions of law on May 2, 1978. Replies were filed on May 16, 1978. Oral argument on the proposed findings was held on May 22, 1978. At my request, the Commission granted me an extension of time to July 3, 1978 to file this initial decision.

This decision is based on the transcript of testimony and exhibits received in evidence, and the proposed findings of fact and replies filed by the parties. I have adopted several findings proposed by complaint counsel and counsel for Coke-New York verbatim. Others have been adopted in substance. All other findings are rejected either because they are not supported by the record or because they are irrelevant.

II. Findings of Fact

A. Coke-New York's Business

1. Coke-New York is primarily a bottler and distributor of various carbonated soft drinks, including Coca-Cola, Fresca, Tab, Sprite, and Fanta flavors under franchise from the Coca-Cola Company; Dr. Pepper and Sugar Free Dr. Pepper under franchise from Dr. Pepper Company; and, Welch's Grape Soda under franchise from Welch's Foods, Inc. (CX 12Z3-5; Tr. 1101).[1] Approximately [6] two-thirds of its sales and earnings are derived from its soft drink business (CX 5C).

2. Coke-New York is a corporation organized, existing and doing business under and by virtue of the laws of Delaware (Ans., ¶ 1) and its home office and principal place of business is located at 411 Hackensack Ave., Hackensack, New Jersey (CX 12A). It first began bottling Coca-Cola in 1910 and is now the largest soft drink bottling company in the United States (Tr. 1101-02).

3. Coke-New York is also engaged in the manufacture of picnic chests, beverage coolers and extruded plastic sheet, the operation of the Delta Queen Steamboat Company (through the Igloo Corporation which was acquired in 1972) and the production and sale of wine (CX 12Z2; Tr. 1099). Its net sales for the fiscal year ending December 1972 were $211,584,000, and they were $189,698,000 in 1971 and $141,549,000 in 1970 (Ans., ¶ 2).

B. Coke-New York's Wine Acquisitions

4. Until 1970, Coke-New York was engaged only in the business of bottling and distributing carbonated soft drinks (CX 12Z2). The company's opportunities for growth in that business were strictly limited by the boundaries of its franchised territories. Thus Coke-New York was faced with the choice of growing by acquisition or not growing at all. In early 1969, therefore, the company decided to investigate acquisitions outside the soft drink business (Tr. 1103). As a result of this decision, Coke-New York acquired Mogen David in 1970, Vermouth Industries of America, Inc. in February 1973 (whose name was changed to Tribuno Wines, Inc.), and Franzia in December 1973 (CX's 5B, 12Z2-3, 6; Tr. 1117).

(1) Mogen David

[1] The following abbreviations are used in this decision:

CX	- Commission Exhibit
RX	- Respondent's Exhibit
Tr.	- Transcript of testimony
Cplt.	- Complaint
Ans.	- Answer
CPF	- Complaint counsel's proposed findings
RPF	- Respondent's proposed findings
CRF	- Complaint counsel's reply to respondent's proposed findings
RRF	- Respondent's reply to complaint counsel's proposed findings

5. Mogen David was Coke-New York's first venture outside the soft drink business. In 1970 it was approached by an investment banking firm and was told that Mogen David was for sale (Tr. 1103). Coke-New York retained two consultants to investigate Mogen David (Tr. 1103–07). [7]

6. In October 1970, Booz-Allen & Hamilton ("Booz-Allen") recommended the acquisition of Mogen David as a "logical first step" in the wine industry:

> The acquisition of Mogen David would be a logical first step for Coca-Cola of New York in positioning itself as a major competitor in the wine industry. Mogen David is the tenth largest firm in the industry and its Concord product line and sweetened wine image should continue to provide steady sales growth and generate attractive after-tax income. The apparent absence of sales problems and financial troubles would permit Coca-Cola of New York to become familiar with the wine industry while earning a reasonable return on its investment (CX 19Z20–21).

7. Both Booz-Allen and Louis Gomberg, a wine industry consultant, recognized the advantages of Mogen David's national reputation and sales force.

> Because of Mogen David's national reputation and product acceptance, existing distributors and retailers would be more likely to handle additional brands and/or products marketed through the firm's sales force as illustrated by the successful entry of MD Double 20 (CX 19Z21). . . .

> . . .the advantages of good sister lines are many - and obvious. Not the least would be more effective use of shipping, distribution and warehousing facilities. Another, improved selling efforts thanks to a larger and stronger sales force. And third, the sales leverage that comes with a demand brand or item.
>
> Because Mogen David itself is a demand item, it in turn could help to move other merchandise in related lines, as well as be helped by some of the other demand items. [8]
>
> Mogen David's present distribution system is among the better setups in the wine industry, exceeded only by Gallo and United Vintners, and pretty much on a par with Taylor and Almaden. It is now served by some of the best wine wholesalers in the country, yet there is room for further improvement in certain markets. One or more other good lines definitely could help in this area (CX 18Z37).

Coke-New York acquired Mogen David in November 1970 (Ans., ¶ 4; CX 55A) by paying $16,750,000 in cash (CX 3R).

(2) Tribuno

8. In February 1973, Coke-New York acquired manufacturing and distribution rights for Tribuno Vermouth from Vermouth Industries of America, Inc., subsequently known as Tribuno Wines, Inc. Distribution of Tribuno Vermouth had previously been handled by Twenty-One Brands, Inc. (CX 5B; Tr. 1116–21; Ans., ¶ 4). Tribuno

Vermouth was then the largest vermouth producer in the United States (CX 11Z7). At the time of the acquisition, Coke-New York ranked fifth in the wine industry (CX's 991, 992).

9. Tribuno Vermouth is produced by Franzia (Tr. 1811–12) and distributed by Mogen David to distributors located throughout the United States (CX's 71B–Z7, 764H; Tr. 1120, 1127).

10. Tribuno Wines, Inc. was acquired by Coke-New York in an exchange of 712,497 shares of Coke-New York common stock. The distribution rights to Tribuno's products were acquired from Foremost-McKesson, the parent of Twenty-One Brands, Inc. for 62,500 shares (CX 11Z1).

(3) Franzia

11. In late 1971 or early 1972, Coke-New York's management concluded that California table wines were "one of the outstanding growth opportunities" and began to look for an attractive acquisition in this business (Tr. 1129–32, 1139, 1182–84). One reason for this search was the belief that Mogen David's business in sweetened and kosher wines was not growing (CX 18H; [9] Tr. 1133). In fact, despite the great increase in wine sales during the past 10 years, its sales of sweet kosher wines have actually declined (RX's 378J, 501).

12. An internal memorandum explains Coke-New York's reasons for seeking the acquisition of a California wine producer.

> The most important reason for Franzia is to enter the growing table wine market and use the quality California premium and generic lines to move across the country market by market to augment the Mogen David universe first and then to complete full national coverage of this line. The obvious reasons for this are to get as much volume into the open states and as many listings in the control states for maximum leverage (CX 680C).
>
> * * * * * * *
>
> The nature of selling through distributors and/or direct in California can reap great benefit for the existing Mogen David lines. It should be possible to use the existing direct sales force to quickly move into the regular Mogen David line, and 20/20 line, the Bear line, and the Jug line. The volume of beverage wine on the West Coast is far greater than we have seen in the balance of the country. Information received indicates that the Gallo and Italian Swiss beverage lines are doing tremendous volumes in major markets within the state of California (CX 680D).

13. In December 1973, Coke-New York acquired Franzia for approximately $40 million worth of Coke-New York stock (Ans., ¶ 15; Tr.1150). At the time of the acquisition, Mogen David was the nation's fourth largest winery, and Franzia ranked seventh. Together, Franzia, Mogen David, and Tribuno made Coke-New York the

third largest wine producer in the United States in 1973 (CX's 991, 992, 996). At the time of the acquisition, Franzia sold and shipped its wine to customers in 41 states and the District of Columbia (CX 12Z14). [10]

14. Franzia is a corporation organized and existing under the laws of the State of California, with its principal place of business located at 1700 East Highway 120, Ripon, California (Ans., ¶ 10).

C. Wine Production and Distribution

(1) Wine

15. Wine is a drink made from the fermented juice of a fruit, usually a grape, although any fruit that contains sugar can be fermented, and if it is fermented, it becomes wine. Fermentation is the chemical change in fruit juice which changes its sugar into alcohol. The sweeter the juice which is fermented, the higher the potential alcohol content of the wine produced. A wine that is bone dry is a wine that has had all of the residual sugar fermented out (Tr. 31–37, 264, 279).

16. Over 90 percent of all wine produced in the nation comes from grapes. Some other fruits which are used to produce wine are peaches, cherries, blackberries and apples (RX 374, pp. 43–45; Tr. 487).

(2) Types Of Wine

17. There are hundreds of different wines sold in the United States (Tr. 325–26, 1339) and, between one year and another, even the same types of wine show significant differences (Tr. 2182–84). The federal government defines wine according to alcohol content for tax purposes. Under this system of classification there are five wine categories:

Still wine with 14 percent or less alcohol ("table wine")

Still wine with over 14 percent and not exceeding 21 percent alcohol ("dessert wine")

Still wine with over 21 percent and not exceeding 24 percent alcohol

Champagne and other sparkling wine

Artificially carbonated wine

(26 U.S.C. § 6041 (b); RX's 378A–Z12, 380A–S; Tr. 561–64)

[11] 18. Table wines (less than 14 percent alcohol) are generally consumed with meals (Tr. 33–34). Dessert wines (over 14 percent

alcohol) are generally, but not necessarily, sweet to the taste (Tr. 232), and although table wines are generally thought of as "dry," some, such as rosé, are sweet to the taste (Tr. 32–33); in fact, some dessert wines are actually drier than table wines (Tr. 34).

19. Sparkling wines are standard table wines which have undergone fermentation by the addition of sugar or grape concentrate. This fermentation produces carbon dioxide which remains in the bottle under pressure and which is the cause of effervescence when the bottle is uncorked (Tr. 39, 561).

20. A separate category of wines is "special natural," that is, herb wines which contain natural flavoring components and non-grape sugar (Tr. 279–80, 561, 596).

21. Wines may also be classified according to the grape from which they are produced. "Varietal" wines, by law, must be made from 51 percent or more of the grape variety whose name they bear. Some varietals are made from 100 percent of the grape variety whose name they bear (Tr. 44–45). Concord wine, which is made from 51 percent or more of the Concord grape is, therefore, a varietal wine (Tr. 471). Varietal wines are considered to have more distinctive characteristics than other wines (Tr. 270).

22. Generic wines are blends of different types of grapes, and are often named after European wine regions. Some generic wines are Burgundy, Chablis, Sauterne (CX's 17H, 19J, 24F, 80B; Tr. 213).

23. Some varietal wines are very distinctive. Louis M. Martini produces a high sugar and low alcohol wine called Moscato Amabile which he believes is different from most other wines (Tr. 2189–90). Canandaigua produces a Scuppernong wine from South Carolina with a sweet, sherry-nutty taste (Tr. 1352–53). Muscatel, produced from the muscat grape, has a sweet, distinct fruity and flowery taste (Tr. 494, 584, 599, 1353–54). Zinfandel has a distinctive berry taste **[12]** (Tr. 59, 598). Gewurztraminer has a spicy taste (Tr. 2978). Concord wine, such as Mogen David Concord, has a very distinctive, "foxy" or grapy taste (CX 964K; Tr. 297, 1320).

24. So-called "pop" wines have enjoyed a recent vogue. These wines (such as Gallo's Thunderbird) made with flavorings (wines made from fruit and berries are not pop wines), may have small quantities of carbon dioxide added to them, have varied alcohol content, and are intended for the young adult market (CX 52Z118–22; Tr. 37, 234–35, 503–04, 595). Often these wines are heavily advertised and promoted as beverage wines, to be consumed other than with meals (CX 52Z118–22; Tr. 546).

25. Kosher wines are prepared under rabbinical supervision and must meet certain standards of cleanliness (CX 18Z22; Tr. 52, 1349,

1423). Otherwise, they are identical to non-kosher wine, both in chemical analysis and taste (Tr. 1349–51, 1423). Vermouth, an aperitif wine, is a blend of neutral white wine and an extract of herbs and botanicals. The extract gives vermouth its distinctive flavor and aroma. Vermouth may be drunk straight or used as a mix in such drinks as a manhattan (CX's 33L, 91R; Tr. 4).

26. Wines are also classified by producers according to their retail price. The industry generally recognizes three price categories: premium and popular priced (Tr. 64) and, in between these, a so-called "mid-premium" (CX 18Z10).

27. Premium wines are priced higher than the popular priced wines. Normally, premium wines come with corks in the bottle and contain expensive labels with art work and high quality paper. Premium wines are usually of a higher quality than popular priced wines (Tr. 341). Premium wines produced in California normally come from grapes grown in its North Coast counties, which include Alameda, Napa, Sonona, and Mendocino (Tr. 38). Eastern wineries such as Taylor, Widner and Gold Seal also produce premium wines (CX 18Z19). The major sources of premium wines are California, New York, France, Portugal, Italy, Germany and Spain (CX 27I).

28. Popular priced wines are sold by such firms as Gallo, United Vintners (Heublein), Franzia, Guild, California Growers, Bear Mountain, East-Side Winery, California Wine Association and Canandaigua (Tr. 64). [13]

29. Mid-premium wines are varietal wines produced from grapes often grown in the San Joaquin Valley. Both producers that specialize in popular priced wines and producers that specialize in premium wines make mid-premiums. Popular price oriented companies that also produce these wines include Gallo, Franzia, California Growers, Guild and California Wine Association. Premium oriented companies that produce mid-premium wines include Almaden, Inglenook, Beringer (with its Los Hermanos brand), Sebastiani (jug[2] wines), Charles Krug (its C. K. Brand) (Tr. 65). Mogen David's wines have been classified as "mid-premium" because of the price range in which they fall (CX 18Z10).

(3) Wine Production, Grape Supply and Land Use

30. Approximately 90 percent of all wine consumed in the United States is domestically produced and about 99 percent of all domestically produced wine is made from grapes (CX 973, p. 42).

31. Wine is produced in the United States from grapes belonging

[2] The term jug wine refers to wines which are bottled in half gallon or gallon sizes, and there is a trend to better quality wines being bottled in these sizes (Tr. 62).

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to two families, the vitis labrusca, which is the native American grapevine and the vitis vinifera, the European grapevine (Tr. 46–47, 278–79, 1345–46).

32. The labrusca family of grapes–of which the Concord grape is a member (42 F. R. 30, 517 (1972)) –is grown mostly in the Northeastern United States, and in particular, in New York, Michigan and Pennsylvania. Grapes from the vinifera family are grown in California, France, Italy and Germany. Although some New York State wineries are experimenting with the vinifera grape, the labrusca grape is more practical in that area because it tolerates colder weather than the vinifera grape (Tr. 1345–46).

33. Hybrid grapes are also grown in the United States, primarily in New York and Michigan. These so-called French-American hybrids are crosses between [14] vinifera and labrusca grapes and represent an effort to produce better quality table wines in cold climates (CX 964K; Tr. 1345–56, 1383–84). Mogen David uses both California vinifera and eastern labrusca grapes and concentrate in the production of its wines (CX's 716Z19, 1041B–C).

34. Wines are produced in every state in the nation (CX 1004F, G, I; Tr. 1370–71); however, California dominates the industry, with some 85 percent of domestic wine output. New York accounts for approximately 8.4 percent of domestic production. Other wine producing states of some significance are Illinois, New Jersey, Virginia, Michigan, Ohio, Washington, Georgia, Arkansas, South Carolina, Missouri, Oregon and Florida (CX 972J).

35. The principal California wineries are E & J Gallo Winery, United Vintners (Heublein), Franzia (Coke-New York), Almaden (National Distillers), Christian Brothers, California Wine Association and Guild Wineries and Distillers (CX 991A). The principal New York wineries are Taylor Wine Company, Monarch Wine Company, Canandaigua Wine Company, Gold Seal Vineyards and Widmer's Wine Cellars (CX 991A; Tr. 1371).

36. Wine producers may grow their own grapes, but they are not limited to that source of supply. Many producers offer bulk wine–that is, wine sold by one winery to another, generally shipped in tank trucks or tank cars (Tr. 331). Producers of popular priced wines are undoubtedly the major customers for bulk wines; however, premium producers may also use them. Sebastiani, a producer of premium wines, converted from bulk sales of premium wines to bottle production beginning in the 1950's (Tr. 2284), as did Mirassou in 1966 (Tr. 2028–30).

37. While most wine makers do not produce every kind of wine, and some specialize in the production of a limited group of wines,

"Wine making is basically a batch process and most of the equipment (crushers, presses, tanks, barrels, pumps and filters) can be used interchangeably no matter what the specific wine type" (CX 27W). Thus, most large wineries can produce any type of wine, even kosher wine, if the grapes are available (Tr. 50, 336, 599, 1423). However, there are legal restraints which prevent the production of certain wines in California. [15]

38. California law prohibits the use of sugar in the production of grape table wines. While California wine producers may add sugar to non-grape wines, sparkling wines, special natural wines,[3] vermouth and formula wines (Calif. Dept. of Health Regs., Tit. 17, Art. 14, §§ 17000–17010 (CX 7888–E, S); Tr. 31, 279–80, 491), California law would prohibit the production of the principal Mogen David products since they are ameliorated by the addition of water and cane sugar (CX's 18Z17, 893A-D; 27 C.F.R. 240.13).

39. The supply of popularly priced wines is tied in to a great extent with grape agriculture. The supply of grapes is controlled primarily by the weather during each crop year and, secondarily, by farmers' plantings; because of this, grape supplies have varied widely over the years (Tr. 251–52).

40. It is impossible for most wineries to escape this cycle for many only own a portion of the vineyards from which their grapes come (RX 27Z5; Tr. 251). Although juice oversupplies might be stored as grape concentrate as complaint counsel contend (see Tr. 29–30), it is apparent that this does not materially alter the relationship between grape oversupply or shortage and wine prices. It is still true that when the grape crop is long, there will be low prices for grapes and for wine (RX's 27E, 194K-L; Tr. 1801, 1252). When the crop is short, there will be competition for grapes and higher prices for grapes and wine (Tr. 387, 1801).

41. If past history is any guide, wine producers will always be faced with periodic gluts and shortages of grapes, with resulting periodic drops and rises in the wine prices (Tr. 122, 251, 573, 2146).

42. When the grape crop is short, as it was in 1972, prices rise sharply (CX 12Z13–14; RX's 27H, 194K-L; Tr. 1252, 1801). The demand for red wine that year exceeded the supply (Tr. 387). Today, the reverse is true; white wine is in tremendous demand [16] and short supply (Tr. 2310) and red grapes and red wine are now cheap (Tr. 2042).

43. In 1973 the crop was very large but inventories were so low that grape prices were bid up and inventory costs were very high

[3] Wine made pursuant to a formula from a base of natural wine, mixed with such things as herbs, spices, fruit juices, sugar, and caramel coloring (27 C.F.R. 240.440).

(RX 378Z11; Tr. 1801). By 1974, the heavy grape plantings of the late 1960's and early 1970's began to yield ever-larger crops (Tr. 898, 1801-02, 2041), with the result that "everybody got killed because there was a glut on the market" (Tr. 1252).

44. Although not all agricultural land is suitable for the production of wine grapes, there is no evidence in the record which would permit an accurate appraisal of the amount of land available in the United States for the planting of grapes which are used in the production of popular or mid-premium wines. The most that can be said is that there appears to be a shortage of land on which premium-wine grapes can be grown (CX's 3H, 24Z5, 27K; Tr. 2310-11, 2178-79),[4] although even this conclusion is tentative, for one small producer of premium wines indicated that he could increase production tenfold by building a facility in the Napa Valley, and expressed no concern over finding the necessary grapes (Tr. 1903-04).

45. The supply of grapes for popularly priced wines is, at this time, more than adequate for producers' needs. Mr. John Franzia of Bronco, a major new entrant, testified that he could buy enough grapes to double his already significant production (Tr. 637). [17]

(4) Advertising of Wine

46. In 1969, the 10 leading wine companies accounted for 63 percent of all wine advertising expenditures. These companies spent 87 percent of all wine advertising money for spot television, 51 percent for network television, 48 percent for newspapers and 43 percent on magazines (CX 19L-M).

47. Several wine companies increased their advertising between 1970 and 1974. Gallo's (the nation's largest wine producer) advertising went from $5.4 million in fiscal 1970 to $10.1 million in fiscal 1974, an increase of 86.5 percent (RX 126A-B). Almaden's advertising expenditures increased 165 percent (RX 36), Canandaigua's increased 203 percent (RX's 62, 66), Guild's increased 146 percent (RX 192A), and Sebastiani's increased 152 percent (RX 351). When Mr. John Anderson took over Sonoma Vineyards, he increased media advertising expenditures from approximately $60,000 to $800,000 (Tr. 1752-53).

48. In 1973, Mogen David had the third largest advertising budget in the wine industry, and it has been among the four or five largest wine advertisers since the early 1950's (CX's 18Z50, 52Z15,

[4] Complaint counsel make much of the fact that it takes from three to five years from planting before grapevines can produce grapes suitable for winemaking (CPF, p. 27) but this would be significant only if there were evidence that at present, or in the foreseeable future, actual or potential wine producers cannot obtain, or will not be able to obtain enough grapes from existing producing vineyards to meet the demand for their products. There is no evidence of this.

Z72). Before its acquisition by Coke-New York, Franzia did not advertise extensively. Its total media advertising in 1973 was $298,691 (CX 716Z15). Since then, Franzia's advertising has increased. In 1975, its planned advertising expenditures were over $1 million (CX 550J).

49. It is not surprising that the wine companies which do advertise believe that it increases their sales (CX's 163B, 782I; Tr. 112–13, 565, 1501) and helps to obtain distributors since they are more likely to take on a wine brand which is heavily advertised (CX's 52Z74, 130B, 136, 337A–B, 405B, 423, 544E; Tr. 437, 566, 645, 1318). Advertising also helps to obtain shelf space in retail stores (CX's 235, 482, 659B; Tr. 1326, 1495). Indeed, advertising by the large wine companies is regarded by industry members as benefitting all wine producers (Tr. 285–86, 505, 1025). Brand identification and distinctive packaging are also considered important contributors to success in marketing wine (CX's 18Z58, 27Z34, 549A–C; Tr. 112, 288–90, 363, 443, 567–68, 1038, 1329–30, 1800, 2055–56, 2311–12, 2176).

50. While it is true that advertising is an important contributor to the successful marketing of wines, there have been several instances where producers [18] have marketed their wines without extensive advertising, and there have been times when well-planned, adequately funded advertising campaigns have failed in their purpose. Thus, it cannot be said that advertising is essential to a wine producer's success. Many other factors, such as quality, price, and reputation are as important as advertising.

51. Several wineries, selling at all price levels from the highest to the lowest, have competed successfully and enjoyed growth with little or no expenditures on advertising. In 1971, California Growers Winery sold virtually no branded case goods (Tr. 362). In 1973, it was not large enough to be included on a list of the 63 largest sellers of wine, the smallest of which sold only 2,998 gallons (CX 991A–B). By 1977, however, the winery sold 600,000 cases of branded products (Tr. 342). California Growers has advertised to consumers only once (spending $1,000 over a three-month period for radio in Puerto Rico), and has never spent more than $15,000 per year in advertising to the trade (Tr. 340, 382–83, 394).

52. California Growers cannot presently afford to advertise more extensively because margins in popularly priced wine are too low (Tr. 346, 384, 388), but Mr. Setrakian, its president, was not sure that he would advertise even if he had the resources to do so, for:

> I can show you as many cases of wineries that have advertised that have gone into bankruptcy as those that haven't advertised that are doing very well. . . . (Tr. 346).

53. East-Side Winery, a small farmers' cooperative, does not advertising but nonetheless sells all the wine it can make (Tr. 248). Gibson Wine Company sold more than 2 million gallons of branded goods and about the same amount of private label in 1976 (Tr. 482, 485). Its sales have nearly doubled since 1973, and had increased more than 105 percent in the six years before that (CX 991A; Tr. 482, 485), yet general manager Marvin Jones testified that Gibson does little advertising and such expenditures for fiscal 1974, the most recent [19] year on record, were less than $40,000, approximately one cent per gallon (RX 161; Tr. 509).

54. Guild, one of the largest wine producers in the country, increased its sales from $13 million to $40.9 million from 1970 to 1974, yet never spent more than $585,000 per year in advertising. Advertising expenses averaged less than 1.2 percent of sales in that period (RX 192A–B). Bronco, a new entrant in the popularly priced end of the wine business, has achieved sales of more than one million cases in three years with no advertising (RX's 50, 51, 52; Tr. 622, 668–69).

55. At the middle price level of wines, advertising is not necessarily a prerequisite to success. Louis Martini, a maker of premium Napa Valley varietal wines, spends less than $10,000 per year on advertising and has no intention of doing any more in the future (Tr. 2161). His long-established company has been profitable in every year and sells in every state except Kansas (Tr. 2146, 2172). In 1977, Martini sold approximately 320,000 cases of wine, about 60 percent more than in 1973 (Tr. 2146, 2178). C. Mondavi & Sons, selling under the Charles Krug and C. K. Mondavi labels, had sales in 1974 of $13.4 million, with an advertising and promotion budget of $79,132, or 0.6 percent of sales (RX's 89E, 90D).

56. Sonoma Vineyards, which does do substantial advertising, has had great success in some markets in which it has done no advertising. In Chicago, for example, sales of 50,000 cases per year–15 percent of Sonoma's nationwide total—have been reached without any advertising but with aggressive pricing and great effort from a single salesman (Tr. 1762–63). Sonoma's president, Mr. John Anderson, was in the advertising business for seven years and worked for sophisticated marketing companies like Norton Simon, Inc. before going to Sonoma (Tr. 1736–37). Even with that background, Mr. Anderson views advertising as only one among many elements (including price, packaging, and manpower) in Sonoma's marketing plans (Tr. 1750–53).

57. After many years in the bulk premium wine business, Mirassou Vineyards entered the branded case goods business for the

first time in 1966 with no consumer franchise (although it did sell some bottled goods from its winery) (Tr. 2029–30). In 1977, sales [20] were 285,000 cases, up 73 percent in the last year alone (Tr. 2033). While the company can afford to advertise, it has never spent more than $6,000 on advertising in a year and has no intention of advertising more substantially in the future (Tr. 2033).

58. Sebastiani Vineyards, perhaps the fastest-growing winery in the United States (Finding 315), has also done very well with little advertising (Tr. 2286). From 1970 to 1974, the years in which Sebastiani's sales "exploded and went off into space," advertising expenditures averaged about $55,000 per year (RX 350; Tr. 2285). Nonetheless, in that time, sales went from 709,000 gallons to 1.2 million gallons (RX 350). By the end of 1977, Sebastiani's sales had reached approximately 5.2 million gallons, an increase of 636 percent in seven years[5] (RX's 350, 351; Tr. 2286).

59. There are several reasons why advertising is not as important in the wine industry as in others. Sebastiani has a tasting room, as do many other wineries, which attracts between 140,000 and 180,000 visitors each year (Tr. 2290), and the impact of actually tasting wines on the decision to purchase them and favorable comments from wine writers is obviously enormous (Sebastiani: "[T]he public relations has done much more for us than advertising") (Tr. 2302).

60. The interest of the general public in wines is evident from the number of publications which report on wineries–and this is all free publicity for the wineries and their wine. Mr. Sebastiani realizes this and invites wine writers to tastings of his wines (and his wife's famous food) (Tr. 2293–95). [21]

> You get people in your house with good food, good wine: It is a nice setting. The wine tastes better, their impression of you is better. . . . So, the wine writers have been invaluable. . .in building the brand. (Tr. 2294).

61. Small wineries like Mt. Veeder Winery also benefit from wine writers. Mt. Veeder has received attention in Gourmet Magazine, Robert Finigian's Private Guide to Wine, New West, Horizon, Westchester, Vintage, Wine World, and even Women's Wear Daily (RX 427A-I; Tr. 1892–1901). Mt. Veeder's only publicity has been through the wine writers, who have made possible the winery's annual sell-out and its steadily lengthening customer waiting list (Tr. 1880, 1888–89, 1902). None of this publicity was sought or paid for by Mt. Veeder; in at least one instance, Mr. Bernstein, its owner, never even met the writer (Tr. 1901).

[5] Sebastiani spent approximately $450,000 on newspaper and magazine advertising in 1977, more than double what had been spent in prior years (Tr. 2312–13). This spending level, however, followed rather than caused Sebastiani's nearly 400 percent growth from 1970 to 1976 (RX 350; Tr. 2286).

62. Like other wineries at both the popularly priced and premium levels, Sebastiani enters its wines in various contests, judgings, and fairs (Tr. 42, 2295). Gold medals, silver medals, and other awards in these competitions are widely publicized. "It helps immensely if you enter a wine competition and it wins some top award and some wine writer picks it up, you can see the sales zoom on it." (Tr. 2295). For example, Mr. Michael Gelven (owner of a liquor store) sought out Giumarra's popularly priced Cabernet Rouge for his store when he learned it had won a medal at the Los Angeles County Fair. Consumers are often aware of medal winners and ask for them (Tr. 2211). Mr. Gelven has sold California Growers Setrakian brand cream sherry, an unadvertised mid-to-low-priced product, on the strength of its medals (Tr. 2237).

63. Together with the growing number of wine writers and publications, publicity from these awards provides a readily available and free alternative or adjunct to advertising and is a significant source of information for the trade and for consumers about new [22] wines and new wineries (Tr. 382, 1333,[6] 1892–1901, 2049, 2076, 2098, 2211, 2237, 2302). As Mr. Gelven's Guimarra episode demonstrates, such publicity is not limited to wines in any particular price category.

64. Just as advertising may not be a prerequisite to success, it may not guarantee success. Mogen David's product Cold Bear was described by Robert Arnold of California Wine Association as a product "[t]hat had a lot of advertising and then an overnight failure." (Tr. 456). Mogen David's Jug had a similar fate, described by a salesman as "impact - then death," and the company was unable to get its advertised new brand Fanfaron out of test markets (CX's 389, 980K; Tr. 1220). Gallo's multi-million dollar campaign for its valley varietals has not made those products a success (Tr. 930–31). Manischewitz's effort to promote its Manischewitz Light wines, with the largest introductory advertising budget in the company's history, has also, in the opinion of some industry members, been unsuccessful (CX 989; Tr. 1222, 2117–18, 2230–31). As long ago as 1952, California Wine Association hired "one of the best" advertising agencies and "spent $400,000 in Los Angeles, at one crack" "[I]t didn't work." For a five-year period ending in 1958, CWA spent more money on brandy advertising in Wisconsin than "all the other domestic brands combined." The result: a sales decline of more than 30 percent (Tr. 157).

[6] One distributor testified that although small wineries might not be able to assist him in making retail contacts and this might hurt its sales "it might work the other way too as far as that part goes. In other words, if it is an exceedingly good product or it is written up in the journals. I mean, you don't need other incentives for somebody to buy it."

65. It is obvious that wine industry members have different opinions about the advertising of their products. Furthermore, even those companies which do advertise more than others do not rely on it as much as members of other industries. In respondent's words, "this is not an advertising-intensive business" (RPF, p. 197). [23]

66. Gallo's advertising expenditures averaged 4 percent of sales from 1970 to 1974 and some of its lower priced brands which sold in the millions of gallons (Carlo Rossi and Paisano) were not advertised at all (RX's 126, 127, 415). Almaden, described as a heavy advertiser (Tr. 346–47), never spent more than 2.1 percent for advertising, and averaged less than 1.8 percent from 1970–74. Its advertising budget averaged $750,000 per year during this time (RX's 36, 361A-G, 362A-G, 363A-K). Canandaigua Wine Company spent some 2 percent of sales on advertising in 1974, mostly on its specialty item, Richard's Wild Irish Rose (RX's 59L, 66A-C). Even the industry's largest advertiser, Gallo, does not spend anywhere near as much for advertising as do leaders in other industries. For example, Gallo's advertising budget for 1974 was half the increase in The Coca-Cola Company's (of Atlanta) advertising budget from 1975 to 1976 (RX's 3I, 126A).

(5) Wine Prices

67. Although the popularity of a particular brand might insulate some wine producers from price competition for a time,[7] there is little doubt that producers of popularly priced wines must compete vigorously if they are to maintain sales. This is especially true for private label business which is intensely price competitive (Tr. 140).

68. The branded business is almost as competitive as the unbranded. Mr. Perelli-Minetti of CWA stated that Bronco (a sizeable new entrant), had "taken their brands" and "priced them at the bottom of the market" by taking advantage of the recent wine glut and buying wine at "20, 30, 40 per cent of cost." According to him, they "raped the industry" (Tr. 144–45). Another witness said "[T]here is no way [he] can meet their prices" (Tr. 1581). Mr. Weibel described Bronco as [24] "the worst" (Tr. 306). Bronco, which does not advertise, relied on price to obtain substantial sales in its first year of existence (Finding 308).

69. Mr. Haas, of East-Side Winery, stated that popularly priced wines are very price competitive, produce low margins and are becoming even more competitive because of the nature of the supplies available for sale (Tr. 245). Mr. Weibel agreed that price is

[7] In his opening argument, Coke-New York's counsel stated that "Franzia regularly has to price its products 10, 20, 30 cents below Gallo because Gallo does have a brand franchise" (Tr. 19).

the key competitive factor in popularly priced wines (Tr. 307), and other industry members agree that in this portion of the business price competition is vigorous (Tr. 335, 470,[8] 509, 559, 2145). This has led to low winery profits (Tr. 399-400, 1208-17, 1756, 1791, 2062, 2190).

70. In Denver, the red wine glut of the mid-1970's drove the consumer price of Cribari gallons to $2.19, far below the regular price of $3.29 to $3.79 and even below the normal promotion price of just under $3.00. Franzia's Denver distributor was forced to respond in order to protect his sales. He did so by cutting regular prices to retailers, running promotions (special discount prices), and cutting his own margins (Tr. 1977). Inglenook, a premium product, owes its popularity in the Denver market to its low prices on gallons (Tr. 2127-28).

71. The Chicago market is also very price competitive at the retail, wholesale, and supplier levels (Tr. 469, 1512, 2073). Retailers are always searching for low-priced bargains, especially unadvertised wines, for the market (Tr. 2104). As a result, distributors selling popularly priced wines are pressed to keep margins low (Tr. 1512). Chicago is Sonoma Vineyards' second largest market in the United States. More than 10 percent of its wine is sold there. Sonoma's Chicago sales were developed by price competition and without any media advertising (Tr. 1754, 1762-63). [25]

72. Price competition may also be used to gain entry into a new market. Bronco entered the St. Louis market-described by Mr. John Simon of Bardenheier as a difficult city in which to obtain distribution-by offering "dirt-cheap prices." (Tr. 1581, 1583-84). Gibson Wine Company is often able to sell its wines to a distributor or chain store because it has an attractive package and "good quality at a very popular price." (Tr. 509). Giumarra Vineyards, which had some trouble obtaining distribution in the price-conscious Chicago market, was able to obtain distribution (the extent of which is not evident) in New York by selling its wine to consumers at 59¢ per bottle (RX 429; Tr. 1497), and Geyser Peak Winery's unadvertised Summit brand was taken on by a Massachusetts retailer because it was priced lower and had a little higher quality than its advertised competitors, Almaden and Paul Masson (Tr. 2219-20).

73. Price invasions are common in the Denver market, where the established popularly priced wines are challenged about every six months by a new wine using primarily price to enter the market (Tr.

[8] Q. When we were talking the other morning, we were talking about the price competition at the branded lower end, you said it's always a rat race at the bottom. Is that an accurate characterization?
A. That is accurate.

1971). C & C Vineyards is often in and out of the market "with a promotion or a low price." (Tr. 2135). Price is so prime a consideration to Mr. Jack Robinson of Argonaut Liquors, Denver's and Colorado's second-largest retailer, that he has purchased low-priced wines without even knowing the name of the winery that makes them (Tr. 2135). Under competitive pressure of that kind, suppliers must keep their prices low; distributors and retailers will spurn them if they are overpriced (Tr. 1993, 2112).

74. As noted above, private label sales, which account for about one-third of Franzia's business are even more price competitive than branded sales (CX 290D; Tr. 246, 385). Private label is sold almost completely on price alone (CX's 550F-G, 559A-B; Tr. 246, 386, 900). Price differences of a nickel or a dime on a case of wine (less than a penny per bottle) shift business from one supplier to another:

> There are times we have been five and ten cents higher and the pressure is tremendous and we don't want to lose the business we have. (Tr. 141). [26]

75. CWA supplies private label wine to the A & P chain and has done so for some years; A & P is CWA's largest private label account (Tr. 170). After a managment change at A & P, "all of [CWA's] friends in the industry that were in the private label business went after A & P as hard as they could." (Tr. 143). Despite customer loyalty they had built up over 10 years, CWA held the business–after a change in management and a year's vacillation by A & P–only by offering the right price (Tr. 142–43). Even so, because lower prices can always be offered, CWA sees Franzia "as a continued threat to [its] retention of that business." (Tr. 175). For CWA, margins on private label wine are "narrow or less than narrow, in the red" and CWA would like to get out of that part of the business (Tr. 141–42). Guild, because of the difference in margin between branded and private label, "decided [it] would prefer to have as little involvement in the private label business as possible. . . ." (Tr. 546–47).

76. Some imported wines may also exert downward price pressure on domestically produced popular wines. New entrants are constantly appearing. For example, during the trial of this case, G. Raden & Sons, a small Seattle distributor-importer, was in the process of introducing a line of popularly priced Italian table wines. Mr. Raden decided to import the wines because he perceived a "dollar quality factor" that created a new opportunity for national marketing (Tr. 1827–32). The wines are priced below $2 per fifth at retail and have already gained distribution or promises of distribution in 10 states (California, Maryland, Massachusetts, New Jersey, New York, Oregon, Rhode Island, Texas, Virginia, and Washington)

and in the Safeway chain in California (Tr. 1830, 1837). Mr. Raden does not intend to advertise them (Tr. 1829). Mr. Raden's importing competitors are large and many of them are subsidiaries of major distillers, but competing with them for shelf space for his new import line does not worry him "because they basically overprice their products and undersell the quality. They are basically not real astute about what they are doing" (Tr. 1831). [27]

77. Nor is Mr. Raden unique as a supplier of low-priced imports. Mr. Michael Gelven sells many low-priced imports in his two Massachusetts retail stores, on of which–an Algerian wine selling for 99¢ a fifth–he characterized as "very passable" quality with "fantastic" sales (Tr. 2223–24). "You can't buy California wine for 99 cents a bottle [in Massachusetts]." (Tr. 2224). Mr. Jack Robinson, co-owner of the second largest liquor store in Colorado, sells many extremely low-priced imports; at the time of his testimony he was having a "great sale" on Italian wine for $1.39 per bottle (Tr. 2106, 2136).

(6) Barriers to the Distribution of Wine

(a) State Regulation

78. Since wine is an alcoholic beverage, its sale is regulated to some extent by every state. In almost every state, wine producers are prohibited from selling products directly to retailers or consumers. Therefore, they must sell their products through distributors (CX 715E). Although virtually all states require the use of middlemen, some, such as New York and Ohio, apply this requirement only to wine produced outside the state. Wine producers in the state may also be wholesalers of wine (Tr. 1290–91, 1440–41). In California, wineries located there may sell directly to distributors and to consumers (Tr. 287, 1936).

79. The states have chosen two major approaches to the distribution of wine. A minority–Idaho, Iowa, Maine, Mississippi, Montana, New Hampshire, Pennsylvania, Utah, West Virginia and Wyoming–operate a state monopoly at the wholesale level. Those states are sometimes referred to as "control states." Alabama, in addition, is a control state for wine of over 14 percent alcohol and a license state for wine of 14 percent alcohol or less. Michigan is a control state for wine of over 16 percent alcohol and a license state for wine of 16 percent alcohol or less. Virginia and Washington State have dual systems, with both the state and the private sector operating concurrently. The remainder, 36 states and the District of Columbia,

license private entities for the wholesaling of wine, and are [28] known as "license states," Tit. 29, § 24, Code of Ala., in CCH, *LCLR,*[9] *Ala.* at ¶¶ 7089A-C. CCH, *LCLR, Ida.* at ¶ 1,230. CCH, *LCLR, Iowa* at ¶ 1. CCH, *LCLR, Me.* at ¶1. § 4363, Mich. Comp. Laws, in CCH, *LCLR, Mich.* at ¶ 7041. CCH, *LCLR, Miss.* at ¶ 1. CCH, *LCLR, Mont.* at ¶ 1. CCH, *LCLR, N.H.* at ¶ 1. CCH, *LCLR, Pa.* at ¶ 1. CCH, *LCLR, Utah* at ¶ 1. CCH, *LCLR, Va.* at ¶ 1. CCH, *LCLR, Wash.* at ¶ 1. CCH, *LCLR, W.V.* at ¶ 1. CCH, *LCLR, Wyo.* at ¶ 1.

80. To do business in the control states a wine producer must first obtain a listing for each label and each variety it wishes to sell. Then he may sell wine to the state, which acts as distributor (Tr. 67, 368). It is more difficult for a wine producer to obtain entry into a control state than in a license state (Tr. 67–68, 545, 1365–66) and it may be even more difficult for a new winery to obtain a listing in a control state than an established winery (Tr. 287, 368–69, 545, 1365). Mr. Setrakian of California Growers testified that in control states the historic relationship between the state board, the winery and the consumer makes the system difficult to break into. In fact, his company has been trying for years without success to get permission to sell its wines in Pennsylvania (Tr. 367–69).

81. As a result of state regulation, corrupt practices such as kickbacks or bribery to obtain distribution and retailer cooperation are fairly common in the wine industry[10] (CX 19Z16; Tr. 186–88, 196–99, 215, 287, 2254–55).

82. Many states have "at rest" laws requiring that wine purchased by a distributor actually be sent to and come to rest on his premises. Examples are the [29] States of Arkansas, Connecticut, Delaware, Florida, Georgia, Illinois and Massachusetts. Such a requirement means that wine cannot be physically shipped from the producer to the retailer without first going to the distributor. § 48-303(c), Ark. Stat., in CCH, *LCLR, Ark.* at ¶ 7086. § 12-436, Conn. Gen. Stat., in CCH, *LCLR, Conn.* at ¶ 7024. Tit. 4, § 501, Del. Code, in CCH, *LCLR, Del.* at ¶ 7101. § 561.24, Fla. Stat., in CCH, *LCLR, Fla.* at ¶ 7193. Ga. Alcohol Reg. 560-2-6-.10, in CCH, *LCLR, Ga.* at ¶ 407.6D. Art. VI, § 7, Ill. Liquor Control Act, in CCH, *LCLR, Ill.* at ¶ 7116. Chap. 138, § 17, Mass. Gen. Laws in CCH, *LCLR, Mass.* at ¶ 7074B.

83. Some states require that a distributor buy wine only from the business entity that the producer has indicated to be the primary source for that wine. Such a law prohibits one distributor (unless he

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[9] *Liquor Control Law Reporter.*

[10] The Booz-Hamilton report noted, however, that these practices should decline as the industry matures (CX 19Z16).

is the designated primary source) from selling his wine to another distributor. States with a "primary source" law include Arkansas and Colorado. § 48-305, Ark. Stat., in CCH, *LCLR, Ark.* at ¶ 7089. § 12-47-128, Colo. Rev. Stat., in CCH, *LCLR, Colo.* at ¶ 7225.

84. Many states prohibit a wine producer from owning or having any financial interest in a wine wholesaler or retailer. Examples are the States of Alabama, Arizona, Colorado, Delaware, the District of Columbia, Florida, Georgia, Illinois, Michigan (in Michigan the requirement applies only to wines of 16% alcohol or less; Michigan is a monopoly state for high alcohol wine), and Ohio. Those same states prohibit a wine retailer from owning or having any financial interest in a wine wholesale operation. § 41, Title 29, Code of Ala., in CCH, *LCLR, Ala.* at ¶¶ 7147-7153. § 4-244, Ariz. Rev. Stat., in CCH, *LCLR, Ariz.* at ¶ 7174. §§ 48-309 and 48-908, Ark. Stat., in CCH, *LCLR, Ark.* at ¶¶ 7097, 7466. § 12-47-129, Colo. Rev. Stat., in CCH, *LCLR, Colo.* at ¶ 7227. Rule 44, Regs. of Del. A.B.C. Comm., in CCH, *LCLR, Del.* at ¶ 4140. § 25-113, D.C. Code, in CCH, *LCLR, D.C.* at ¶¶ 7066-7067. §§ 561.24 and 561.42, Fla. Stat. CCH, *LCLR, Fla.* at ¶¶ 7132, 7177. Ga. Alcohol Reg. 560-2-2-.15 and 560-2-4-.02, in CCH, *LCLR, Ga.* at ¶¶ 4028E and 4051. Art. VI, §§ 3(a) and 3(e), Ill. Liquor Control Act, in CCH, *LCLR, Ill.* at ¶¶ 7110 and 7110D. § 436.31, Mich. Comp. Laws, in CCH, *LCLR, Mich.* at ¶ 7123. § 4301.24, Ohio R.C., in CCH, *LCLR, Ohio* at ¶¶ 7184, 7185. [**30**]

85. In Kentucky, the number of wholesale licenses may not exceed one for every 31 retail package liquor licenses, which themselves are limited on the basis of population figures. 804 KAR 9:020, in CCH, *LCLR, Ky.* at ¶ 4245. Since 1964 the Kentucky Department of Alcoholic Beverage Control has issued a total of four new wholesale liquor licenses, one each in 1964, 1968 and 1976 (CX 1015A).

86. Ohio prohibits the awarding of additional franchises for the same brand in the same territory, which is apparently an exclusive territory law with a grandfather clause. Ohio R.C. in *LCLR, Ohio* at ¶¶ 7005B, 7005D, 7005E. One effect of exclusive distributorships is probably higher prices to the retailer and to the consumer; dual distributorships would almost certainly cause prices to be lowered (CX 903; Tr. 1963-64, 2266-67).

87. Some states exert authority over the price charged to consumers. Alabama prohibits a distributor from changing his prices more often than once every 120 days. California has a fair trade law for alcoholic beverages (Tr. 68-69). Connecticut requires a manufacturer to post a schedule of consumer retail prices, although the retailer may sell below that price. Kentucky has a mandatory fair

trade law, which requires that wholesalers and retailers sell at a price stipulated by the vendor. The law also requires a minimum resale price, without discount: the wholesaler must mark up wine at least 20 percent, and the retailer must mark up wine at least 33 1/3 percent if less than a case and at least 10 percent if a case of more is sold. A Massachusetts law requires a wine producer to post a minimum retail price and a retailer must sell at no less than the minimum. New York requires a producer or wholesaler to maintain a minimum consumer resale price for wine. Ohio has both a minimum markup for wholesalers and retailers and a minimum retail price schedule for wine that must be followed by each wholesaler and retailer. Ala. Reg. 28, in CCH, *LCLR, Ala.* at ¶ 4100. § 30-64, Conn. Gen. Stat., in CCH, *LCLR, Conn.* at ¶ 7262. §§ 244.380 and 244.390, Ky. Rev. Stat., in CCH, *LCLR, Ky.* at ¶¶ 7513- [31]7523. Chap. 138, § 25C, in CCH, *LCLR, Mass.* at ¶¶ 7116 and 7116N. N.Y. Alcoholic Beverage Control Law, § 101bbb, in CCH, *LCLR, N.Y.* at ¶ 13187. § 4301.13, § 4301:1103(G), in CCH, *LCLR, Ohio* at ¶ 4131.

88. Other restrictions on price competition exist in those states which control or prohibit the advertising of wine. Alabama prohibits wines over 14 percent alcohol from being advertised on billboards, and prohibits displays. Georgia prohibits all advertising in newspapers, periodicals, or on signs, posters, billboards, or vehicles. Michigan prohibits advertising of any brand outside the premises of a retailer, and prohibits illuminated signs and signs of more than 22 by 28 inches of any brand inside the premises. These states do not prohibit the advertising of wine in the electronic media. Ala. Regs. 21, 22 in CCH, *LCLR, Ala.* at ¶¶ 4068-76. § 58-301, Code of Ga., in CCH, *LCLR, Ga.* at ¶ 7046. Rules 436.68 and 436.69, Mich. Liquor Regs., in CCH, *LCLR, Mich.* at ¶¶ 4121-4124.

89. Advertising the retail price of wine is prohibited in several states, including Arkansas, Delaware, Georgia and Ohio. In Arkansas, the District of Columbia and Georgia, a sign indicating price in a retail store may not be visible from outside the store. § 147, Ark. Liquor Regs., in CCH, *LCLR, Ark.* at ¶ 6449. Rule 27, Del. A.B.C. Comm. Regs., in CCH, *LCLR, Del.* at ¶ 4100. § 5.1, D.C. Regulations in CCH, *LCLR, D.C.* at ¶ 4051. § 58-301, Code of Ga., in CCH, *LCLR, Ga.* at ¶ 7046. Ga. Alcohol Regs. 560-2-8-.01, in CCH, *LCLR, Ga.* at ¶ 4085. § 4301.211, Ohio R.C. in CCH, *LCLR, Ohio* at ¶ 7172A.

90. Cooperative advertising between a retailer and a manufacturer, or between a retailer and a distributor is prohibited in Arizona, Michigan, New York and Ohio. § 4-243, Ariz. Rev. Stat., in CCH, *LCLR, Ariz.* at ¶ 7161. R 436.1319, Mich. Liquor Regs., in CCH, *LCLR, Mich.* at ¶ 5119. CCH, *LCLR, N.Y.* at ¶ 13087-08. Ohio Regs.,

Liquor Control Comm., § 4301: 1-1-44(f), in CCH, *LCLR, Ohio* at ¶ 4450.

(b) Difficulties in Obtaining Distribution

(1) *Distributors*

91. Distribution is important–even "crucial" in the words of one producer, to success in the wine [32] industry (CX 36A; Tr. 157–59, 347, 428, 548, 1555) and many wine companies have representatives who call on wholesalers to convince them to purchase their wines and to educate the wholesaler's salesmen about those wines (CX's 195A–B, 222A–B; Tr. 111–12, 300–01). Representatives of the larger wine companies reinforce their distributors' sales efforts by calling on retailers and restaurant accounts (CX's 27Z51, 138, 143, 228, 373, 377; Tr. 112, 138, 300–01, 569–70, 978).

92. Many wineries employ salesmen, an advantage which smaller wineries may not be able to afford (Tr. 364, 416–17). A study prepared for Coke-New York by Arthur D. Little reported:

> All of the larger marketers. . . employ sizeable sales forces to call on wholesale customers and also accompany wholesale salesmen on their calls to retailers. This is a major marketing expense but a necessary expense if the marketer wishes to obtain shelf space in retail stores. Small producers cannot afford this expense and as a result, they rely heavily on demand-pull. They also rely heavily on selected distribution rather than attempting to obtain wide distribution. (CX 27Z34).

The Little study also claims that large wine producers are able to "pull" products through a wholesaler by using their salesmen and advertising, something which smaller producers with a more restricted advertising budget and few or no salesmen might not be able to do (CX 27Z48–49).

93. Several industry witnesses testified that distribution is becoming more difficult because the number of distributors–or, at least "good" distributors – has declined (Tr. 219, 298, 348–49, 427, 548, 551, 1297, 1359–61, 1555). A good distributor is one who has a personal interest in the producer's brand, is able to develop resales on a volume basis, a wine division, a good credit rating, and a well-trained sales force (Tr. 93–94, 348, 430, 548, 1359, 1750). According to some witnesses, there may be no more than four or five "good" distributors, and in smaller cities there may be only one or two (Tr. 100, 430–31, 550, 1360–61, 1555). [33]

94. Difficulty in finding a distributor may also be created by exclusive distribution, *i.e.,* by a producer limiting his wine line to one distributor in a given area (Tr. 1048, 1496–97, 2008). The distributor,

in turn, will often be reluctant to take on a competing producer's line or to devote much time to it (CX 27Z48).

95. This has been the experience of some producers. California Growers finds it difficult to get into a good wholesale house where there are comparable brands (Tr. 348–59), as does CWA (Tr. 81, 128). Canandaigua finds that if a distributor is effective with one supplier's brand he is reluctant to accept and promote a competing brand (Tr. 1364), and in one instance one of Coke-New York's salesmen offered the Franzia line to a distributor who ". . .refused it out of fear of reprisal from Guild" (CX 601).

96. Producers, including Mogen David and Tribuno, also believe that having a broad line of products helps them in obtaining distribution (CX's 161, 770H–I; Tr. 214, 293, 434), and they emphasize this fact in advertisements to the trade (CX's 961, 963, 966, 971).

97. The importance to Mogen David of broadening its product line to include several new wine products was recognized in an early 1970's report:

> Our objective for some time has been to move up into the position of the top three or four wine marketers. In order to have leverage with distributors to attain the third or fourth spot, it is mandatory that we enter into the volume market that the 11% wine category presents. If we can market successful products in all categories of the wine industry and develop substantial volumes, we can then create a major wine selling force in most of the urban areas in the U.S. (CX 23A–B).

98. Other difficulties which may be faced by a producer seeking expanded distribution are the tendency of distributors to favor existing producers by taking on their new products (Tr. 125–26, 1438–39, 1567) to favor large producers with a national brand (Tr. 117, [34] 217–18, 1364, 1453, 1555) and producers who promote their products (Tr. 92–93, 291–3, 373–74, 430, 645, 1362–63, 1575).

A 1972 Arthur Little study on the U.S. wine market concluded that:

> . . .distribution problems favor existing suppliers over new entries. (CX 27L).

99. However, despite the perceived shortage of good distributors, and other distribution problems, several wineries have obtained distribution in recent years (RX 57A–B; Tr. 214, 248, 1363–64, 2031, 2296, 2309–10). Mirassou Vineyards, starting from no base in 1966, has acquired 150 distributors in a 10-year period (Tr. 2031). Sebastiani Vineyards, which has 290 distributors in every state except Mississippi, acquired approximately 240 of them since 1970 (Tr. 2296, 2309–10). With no active effort to do so, Bronco has been able to obtain distribution in [see *In Camera* Findings] states and [see *In Camera* Findings] (RX's 50E–G, 51E, 52E–F; Tr. 637–38). Mt.

Veeder Winery, probably as small as any in the country, has distribution in at least eight states and could easily obtain more distribution if it produced more wine: It has a long list of would-be customers (Tr. 1901-02, 1906-07).

100. Examples of successful distribution are not limited to Coke-New York's witnesses. Although complaint counsel's witnesses testified generally about difficulties in obtaining distribution, there is no specific evidence that most wineries are unable to obtain adequate distribution in any particular trade area.[11] Many producers witnesses testified that, although they might want more, they have been able to obtain distribution. Six-year-old California Growers Winery has amassed 115 distributors for its branded products in 29 states, Puerto Rico, and the Virgin Islands (RX 57Z-B). California Wine Association, [35] despite generally declining sales, has "very much better" distribution now than it did 15 years ago (Tr. 159). Canandaigua Wine Company has 300 distributors (Tr. 1363-64). East-Side Winery, a cooperative with no advertising budget and no well-known brands, does not need more distributors because the ones it has are selling all the wine it can make, 2.5 million gallons (Tr. 214, 248). East-Side has five distributors in Wisconsin alone (Tr. 214, 222, 248). Despite the limited number of distributors there and in North Dakota and South Dakota, East-Side's general manager said, "I think that for the most part I am in houses I would like to be in. If I could not be there, there are others I would be satisfied to be associated with." (Tr. 222).

101. Weibel has about 100 distributors, in more than half the states (Tr. 286-87, 320). Gibson has distribution in 36 states (Tr. 500). Guild has 340 distributors, giving it distribution in all but six or seven states (RX 194E; Tr. 544). C. Mondavi & Sons, a small family company that does almost no advertising, had 104 distributors in 1974, covering all but five states (RX 91B-C). Concannon Vineyard, also a small family company that does almost no advertising, had 63 distributors in 1974, 26 in California and 37 in 27 other states (including six control states) (RX 92E-J).

102. Although the number of liquor-dominated distributors may have declined in some markets, available distribution for wine has not been reduced substantially. Mr. Perelli-Minetti explained that this is so because liquor distributors have been setting up wine divisions and making a real effort to go after wine volume and because "there are tiny houses springing up" and these small houses,

[11] Messrs. Simon and Perelli-Minetti did testify that they have found it difficult to find another distributor when they lost one in a market (Findings 269, 271), but this problem has not been met by other producers who may be more competitive than Bardenheier and CWA.

with relatively fewer salesmen but salesmen who concentrate on wine, may do a better job for a winery (Tr. 100–01).

103. In view of the nation's increasing interest in wine,[12] it seems inevitable that businessmen will enter into its wholesale distribution. In the State of Washington, for example, the distributor G. Raden [36] & Sons was established in 1972 and has grown to a nearly $4 million business (Tr. 1816, 1824). While a student in law school, Mr. Gary Raden obtained, for $350, a license to import and distribute wine and beer and he began doing business (Tr. 1815–16). His resources were a rented 2,000-square-foot space in the basement of a second-class hotel, one truck, between $7,000 and $10,000 in capital, and himself as the sole employee (Tr. 1817–18). In his first year, he sold between 300 and 500 cases of wine per month with total sales of less than $100,000 (Tr. 1818).

104. Two years later, having spotted what he thought was an opportunity in the expanding Washington market, Mr. Raden approached Franzia and took on a secondary Franzia brand called Yosemite Road. Franzia had not been sold in the market before (Tr. 936–37, 1819). Mr. Raden's distributorship business grew and he left law school in 1975 to devote full time to it (Tr. 1842–43). His company now sells between 16,000 and 20,000 cases of Franzia wine per month to 600 retail accounts, and also smaller amounts of Beringer, Sebastiani, Mt. Veeder Winery, and Sutter Home Winery products (Tr. 1821–22). All of the wines he sells were obtained as a result of his requests to the suppliers (Tr. 1819, 1822).

105. Today, Mr. Raden's 10,000-square-foot warehouse is too small and 37 employees, 11 trucks, and a computer are needed to operate his business (Tr. 1823–24). Although headquartered in Seattle, Mr. Raden covers the entire western part of Washington. G. Raden & Sons is and always has been profitable (Tr. 1823–24).

106. Although Franzia accounts for 60 percent to 75 percent of Raden's sales, and Mr. Raden credits Franzia with the growth of his business, he is confident that even without Franzia he could have become a substantial figure in the Washington distribution business because [37] he could have built his business with any other properly priced brand not then in the market (Tr. 1824, 1832–35).

107. Mr. Raden's success, and Franzia's, were achieved without advertising (before October 1977) and without service, support, training, or manpower from the winery (Tr. 1844–45). Instead:

We spent a lot of time knocking on doors. Gaining distribution is not the easiest

[12] Per capita consumption in the United States has been increasing steadily over the past several years (Finding 329).

thing in the world but with a degree of persistence and a product that is good quality price-wise, you can achieve major distribution. (Tr. 1818).

108. Denver has also seen new entrants in wholesale distribution. Three new distributors of California and imported wines have recently been established: Lido, Dionysus, and Windsor (Tr. 1975). Windsor obtained the Sonoma Vineyards line when Sonoma decided to add a second distributor in the Denver market (Tr. 1994-95, 2112). An alternative to traditional wine distribution channels is also developing in Denver. One food wholesaler is presently selling wine and a second is beginning to do so (Tr. 1975). A distributor competitor of these two new entrants described their importance this way:

It is relatively early to say at this point. I think they are learning the business and it is going to take them a while to learn it, but they have got salesmen and their trucks go to the shops presently, so they are definitely a factor to be contended with. (Tr. 1975).

109. In Los Angeles, food brokers are also entering the wine distribution business (Tr. 940-41). Franzia sells 10,000 cases per month through Doug Bradshaw, a food broker there who had previously had only a token wine operation (Tr. 940-41). Use of food brokers for wine distribution may well grow, as more states are permitting supermarkets and grocery stores to sell wine (Tr. 74). Such stores, which have always been serviced by food brokers, are devoting an increasing share of shelf space to wine–perhaps as much as tenfold in some cities (Tr. 73, 396, 568, 911). [38]

110. Although several producers question their ability to sell wine, beer distributors are beginning to show interest in wine distribution[13] (CX 27Z55; RX's 194E, 245, 262, 265, 278, 279;[14] Tr. 242, 944-45) and provide an alternative (although perhaps not completely satisfactory to some producers) to traditional wine distribution.

111. Beer distributors vary in their ability to sell wine, as do all other wine distributors (Tr. 357, 549, 2217). However, there is no reason why beer distributors cannot do an adequate job of distribution for some wineries. In fact, Gibson Wine Company prefers beer distributors to liquor distributors because the fit between most beers and popularly priced wines is good, both being high-volume and low-price/low-margin products (Tr. 519, *see* 314). Mr. Louis Martini, who

[13] The Arthur Little study of six years ago noted that beer distributors' share of the wine distribution business was increasing (CX 27Z46).

[14] A Monarch wine salesman reported:

I spent two days at the state's annual beer convention. In addition to seeing several of our distributors there, I also met and spent some time with men that are only in the beer business; for the time being anyway. These are the beer distributors in the various areas, that are planning on getting into the wine business.

knows little of his company's distribution operations, nonetheless knew of at least one beer distributor that is performing well for his premium winery (Tr. 2149–50). In the view of Mr. Robert Ivie:

> There are some distributors who have beer and distilled spirits lines who are competent or good because of that. There are others that have those things that are not competent because they have them. So I don't think there is any general rule . . . . (Tr. 549).

[39] 112. Canandaigua Wine Company has used beer distributors for some of its products (Tr. 1361–62). Mr. Marvin Sands thought it "hard to generalize" about their ability, but he testified that some beer distributors have done well for its proprietary specialty products (Tr. 1361).

113. Selling a broad line of California wines, California Growers Winery has a similarly particularized view of beer distributors. Mr. Robert Setrakian said, "I think that the quality of a given beer distributor for the distribution and sale of wine is dependent on the quality of ownership of that distributing house." He cited as an example one beer distributor in northern California that distributes his Growers brand and does an excellent job; and, in contrast, a beer distributor in Chicago that on a population basis did a "lousy job" (Tr. 357).

114. From 20 percent to 25 percent of the beer distributors in Cleveland carry wine (Tr. 1296). Beverage Distributing Company, for example, carries Roma wine and Miller and Stroh's beers (Tr. 1335). Franzia's Cleveland distributor, American Vineyards, also distributes beer (Tr. 1335). In Massachusetts, beer distributors also sell wine, including such prominent brands as Almaden (Tr. 2216–17).

115. One of the major wine distributors in Denver, Mr. John Pearson's C & C Distributing, is also a major figure in beer distribution (Tr. 1966–83). Mr. Pearson bought C & C Distributing, a small distributorship, in 1972 (Tr. 1967). When he came to work, with no previous experience in distribution, the company employed one salesman and sold less than $1 million per year (Tr. 1966). Since then the business has grown roughly fourfold and now employs 10 salesmen. By volume, half of the business is beer and half wine (Tr. 2000). The same sales force sells both beer and wine, including 6,000 cases per month of Franzia (Tr. 1968, 1974).

116. Beer distributors have been and remain important to Franzia. Of Franzia's branded business, 35 percent is sold through 13 distributors: 11 of the 13 are **[40]** beer distributors (Tr. 936–47). Of the two others, one is now entering the beer distribution business (G. Raden & Sons), and one is a food broker (Doug Bradshaw, Los

Angeles). In addition to C & C Distributing in Denver, 10 beer distributors have developed substantial wine distribution capability with Franzia products (Tr. 936–47). Franzia's commitment to these distributors was minimal, only some training and advice (Tr. 977–78). Advertising was not promised, merchandising materials were usually no more than a few posters, and Franzia did not underwrite the distributors' costs of training (Tr. 980–83).

117. Despite the feelings of some wine producers that beer distributors might not do a good selling job, retailer witnesses said they were willing to deal with any and all distributors (Tr. 2080, 2110, 2215–16). None stated any objection to beer distributors; and one, Mr. Michael Gelven, specifically said that beer distributors are "as competent or as incompetent" as any other distributors (Tr. 2217).

118. Another alternative to traditional distribution is "clearing," the process under which a distributor, while satisfying state law, does no more than clear the wine through his warehouse, taking delivery from the supplier and transferring the wine to the retailer for a fee (Tr. 1963, 1976). Mt. Veeder Winery, for example, clears some of its wine through distributors (Tr. 1963). One distributor who testified said that he clears all kinds of wine "every month" (Tr. 1976). All of the retailers who testified said that the ease of clearing products not in general distribution enables them to obtain any product they wish to sell (assuming the winery has enough to supply them) (Tr. 2079–80, 2113–14, 2211–12).

119. Michael Gelven, a retailer in rural southeastern Massachusetts, noted that if he is successful with a product that has been cleared for him and re-orders it, the distributor may begin to carry the product in inventory for sale to other retailers (Tr. 2212). Since most wine products are already regularly available in Massachusetts from one of the 27 distributors with whom Gelven deals, only 3 percent to 5 percent of his business involves the clearing process (Tr. 2273). [41]

120. Clearing may also be used in private label sales. For example, Mario Perelli-Minetti testified about California Wine Association's direct courting of the A & P account, a national account,' although the wine was sold through distributors like Continental in Chicago (Tr. 121, 133–34, 170–75, 453).

121. There is a dispute between the parties as to the number of active or potential distributors available to wine producers. Complaint counsel relied on guesses by their witnesses which were not backed up by any hard evidence and which were, in some cases, inconsistent. Mr. Ivie, for example, guessed that "[t]here might be 30

or 40" distributors in Wisconsin; Mr. Ernest Haas thought there were maybe 20 (Tr. 222, 554), yet CX 1031 lists more than twice that number actually selling wine to retailers in 1976. Mr. Marvin Sands was asked how many distributors there are in an "average metropolitan area" and stated, for Cleveland, that there are one or two "good" distributors and a few others (Tr. 1360), but Mr. Fred DePompei, who is a Cleveland distributor, testified that there are between 15 and 20 active wine distributors in his city (Tr. 1334).

122. Guesses by complaint counsel's witnesses do not provide reliable evidence of the number of distributors available to wine producers. The evidence offered by Coke-New York[15] (together with rebuttal evidence by complaint counsel) is a much more reliable indicator of the availability of wholesale wine distribution in the 20 states which account for 77 percent of all wine consumption and 82 percent of all wine consumption where distribution is not a state monopoly (RX 380H). The following list of distributors shows those which are licensed and those which are actually distributing wine. Where distributors have paid substantial license fees, but there is no evidence that they are actually distributing wine, I believe it is not unreasonable to assume that they are potential distributors.

123. Arizona has 89 distributors licensed to sell wine: 65 licensed for wine, beer, and spirits, 24 licensed for wine and beer. Each has paid an application [42] fee of $50, a license issuance fee of $1,500, and an annual fee of $100 or $250 (RX's 430B, 431E–H) Twenty-three of those licensed (one for every 67,000 adults) are presently active in distributing wine (Stat. Ab. 28;[16] CX 1010).

124. California, in which the state's many wineries may themselves sell directly to retailers, has 749 distributors licensed to sell wine (RX's 432B, 433D).

125. Colorado has 18–20 active distributors selling wine to retailers (Tr. 1974, 2110). Each distributor has paid an annual license fee of $1,000 (Col. Rev. Stat. §§ 12–47–115 and 123). Mr. Pearson of C & C Distributing in Denver, estimates that he covers 90 percent to 95 percent of the state's population (Tr. 1980).

126. Florida has 199 distributors licensed to sell wine: 46 licensed for wine, beer, and spirits, 153 licensed for wine and beer (RX 434A–B). Each has paid a substantial license fee and posted a bond for at least $1,000; 46 have paid an annual fee of $4,000 and 153 have paid an annual fee of $1,250 (Fla. Stat. § 561). Seventy-three of those licensed (one for every 84,000 adults) are presently active in distributing wine (Stat. Ab. 28; CX's 1011, 1012B).

[15] Obtained from officials supervising their state's licensing activities.

[16] U.S. Bureau of the Census, Statistical Abstract of the United States 1977.

127. Illinois has 448 distributors licensed to sell wine, beer, and spirits, each of which has paid an annual fee of $150 (RX's 435A, 436B–H). One hundred eighty-six of those licensed (one for every 42,000 adults) are presently active in distributing wine (Stat. Ab. 28; CX 1014).

128. Kentucky has 31 distributors licensed to sell wine and spirits, 25 of which are active in distributing wine, and each of which has paid an annual fee of $1,000 and posted a bond for at least $2,000 (Stipulation dated March 17, 1978; CX 1015G; RX 437A, E; Ky. Rev. Stat. § 243). Although the number of distributors in Kentucky is limited by state law, the limitation does not appear to be significant since it does no more than limit the number to one distributor for each 77,500 persons, including children (CX 1015).

129. Louisiana has 47 distributors licensed to sell wine (RX 438). [43]

130. Massachusetts has approximately 50 active distributors selling wine to retailers (Tr. 2242). Each distributor has paid a substantial annual license fee: $5,000 for those who sell wine and beer (Mass. Gen. Laws Ann. Ch. 138 § 18). In rural southeastern Massachusetts where he operates two retail stores, Michael Gelven is serviced by 27 distributors located in eastern Massachusetts (Tr. 2214–15). One of those distributors is located 70 miles from Mr. Gelven, in Lawrence, Massachusetts (Tr. 2217).

131. Michigan has 263 distributors licensed to sell wine and beer, each of which has paid an annual license fee of $300 plus $50 for each delivery truck in use (RX 439C–I). One hundred eighty-one of those licensed (one for every 34,000 adults) are active in distributing wine (Stat. Ab. 28; CX 1018).

132. New Jersey has 153 distributors licensed to sell wine, each of which has paid a substantial license fee (RX's 440A, 441E). Of these, 78 have paid an annual fee of $7,000, 56 have paid an annual fee of $1,500, and 19 have paid an annual fee of $3,000 (*Id.*).

133. New York has 202 distributors licensed to sell wine: 116 licensed for wine and spirits, 86 licensed for wine only (RX's 442T, 443B–C). Each has paid a substantial license fee: 116 have paid an annual fee of $5,000 and 86 have paid an annual fee of $625 (N.Y. Alc. Bev. Cont. Law §§ 62, 66(3), 78(1), 83(2); RX's 442T, 443B–C). One hundred seventy-nine of those licensed (one for every 72,000 adults) are presently active in distributing wine (Stat. Ab. 28; CX 1019). Second-ranked in total wine consumption, New York has seen a 63 percent increase in the number of active wine distributors in four years, from 110 in 1973 to 179 in 1977 (CX 1019; RX 380).

134. North Carolina has 61 distributors licensed to sell wine (RX 444A–Z11).

135. Ohio has 154 distributors licensed to sell wine, each of which has paid a license fee (RX's 445, 446B–C). Of these, 30 have paid an annual fee of $100 and 124 have paid an annual fee of $500 (*Id.*). In Cleveland alone, there are between 15 and 20 distributors active in distributing wine (Tr. 1334).

136. Oregon has 133 distributors licensed to sell wine, under 104 separate ownerships (CX 1021; RX 447). Each of them has paid an annual license fee of $275 and posted a bond of at least $1,000. [44]

137. Rhode Island, the nation's smallest state, has 17 distributors licensed to sell wine: 16 licensed for wine, beer, and spirits, one licensed for wine and beer (RX's 448A–B, 449B–C). Each has paid a substantial license fee: 16 have paid an annual fee of $3,000 and one has paid an annual fee of $1,250 (RX's 448A–B, 449B–C). Thirteen of those licensed (one for every 51,000 adults) are presently active in distributing wine (Stat. Ab. 28; CX 1023).

138. South Carolina has 78 distributors licensed to sell wine and beer, each of which has paid an annual license fee of $400 (S.C. Code §§ 61–9–10 and 310) (RX 450).

139. Texas has 154 distributors licensed to sell wine anywhere in the state and 64 licensed to sell wine only in the county in which they are located. Of the 154 all-state distributors, 49 are licensed for wine, beer, and spirits and have paid an annual fee of $1,250; 105 are licensed for wine and beer and have paid an annual fee of $200; the county wholesalers are licensed for wine and beer and have paid an annual fee of $50 (RX's 451R, 452). Sixty-eight of those licensed (one for every 125,000 adults) are presently active in distributing wine (Stat. Ab. 28; CX's 1025A–B, 1029).

140. Virginia has 55 distributors licensed to sell wine, each of which has paid an annual license fee of at least $450 and posted a bond of at least $5,000 (Va. Code §§ 4–25(g), 4–31(g), 4–33(b); RX 453).

141. Washington has 140 distributors licensed to sell wine, each of which has paid an annual fee of $250 (RX's 456D–E, 457B–C). Licenses are issued only to those having an actual commercial intent to enter the distribution business (Tr. 1840–41).

142. Wisconsin had 88 distributors who sold wine to retailers in 1976 (CX 1031). Of 106 firms reporting such sales, 18 were identified as wineries, leaving 88 who are distributors (CX 1030).

143. In these 20 states, some 3,195 distributors are licensed to sell wine. In 11 states, with 1,625 licensees, 904 distributors are presently active in [45] selling wines, and others are potential wine distributors. For the remaining 9 states, with 1,570 licensees, complaint

counsel did not present any evidence disputing the data provided by state officials and it must be assumed that many of them are also active in selling wine.

144. Complaint counsel argue (CRF, pp. 35-37) that these numbers are deceptive, for many distributors (for example, a girls' high school (RX 454B-F)) may not be engaged in commercial activity or, if they do, may be so small that they cannot do an adequate job. I agree with complaint counsel that "the only important consideration is the number of distributors that are commercially viable" (CRF, p. 37) but they lose sight of the fact that since they claim that there is a scarcity of "good" distributors, it was their burden to come forward with reliable evidence of that scarcity. Instead, they presented vague and contradictory estimates.

145. The importance of Coke-New York's evidence lies in the fact that, while it does not reveal precisely how many distributors of wine there are, it provides a reliable basis for two conclusions: (1) That there are many actual or potential distributors available for wine producers and (2) That complaint counsel's claim that wine producers are, or will be, faced with an inadequate distribution network has not been established.

(2) *Retailers*

146. Wine may be sold for off-premise consumption in supermarkets, package stores (liquor stores), and, in monopoly states, in state owned stores (CX 2H; Tr. 365, 368, 1501, 1569), and all wines compete with each other and with other products for shelf space in these stores (Tr. 323-24, 364, 395-96, 476, 1327, 1330, 1498, 1957, 2391). However, some states, such as Colorado, Connecticut, Florida, Georgia, Kentucky, and New York prohibit the sale of wine in stores where food is sold. §§ 12-47-116 to -117, Colo. Rev. Stat., in CCH, *LCLR, Colo.* at ¶¶ 7201-7202, § 30-20, Conn. Gen. Stat., in CCH, *LCLR, Conn.* at ¶ 7165. § 565.04, Fla. Stat., in CCH, *LCLR, Fla.* at ¶ 7278-C. Ga. Alcohol Regs. 560-2-5.02, in CCH, *LCLR, Ga.* at ¶ 4057. § 243, Ky. Rev. Stat., in CCH, *LCLR, Ky.* at ¶ 7274. § 63, N.Y. Alcoholic Beverage Control Law, in CCH, *LCLR, N.Y.* at ¶ 11611. **[46]**

147. There is a trend, however, among the states to permit wine sales in supermarkets (CX 2H; Tr. 73)-a trend which is opposed by package stores, the traditional source of wine[17] (Tr. 73).

148. In states where it is legal, supermarkets are significant sellers of wine, and their contribution to retail sales has increased substantially over the past 10 years (CX 2H; Tr. 1329, 1569). When a

[17] For example, package store owners have prevented passage of a law in New York which would permit supermarket package sales (tr. 73-74, 1377).

state removes restrictions on supermarket sales, wine sales increase (CX 27Z54; Tr. 74).

149. Because they have less shelf space to devote to wines than do package stores, supermarkets, according to some industry members, carry a smaller variety of wines (Tr. 117, 1330, 1500), and there is some evidence that supermarket personnel may be more interested in fast-moving, advertised wines (CX's 2H, 5Q; Tr. 118).

150. The facts recited above, do not, however, lead to the conclusion that smaller wineries have more difficulty in obtaining retail distribution than larger wineries. Perhaps supermarket personnel do favor larger, more heavily advertised wines, but their job is to satisfy customers and if a wine becomes popular for some reason other than advertising (for example, an extremely low price), it is inconceivable that they would refuse to handle it.

151. Furthermore, the number of retail outlets for wine is enormous–some 342,000 (a number which has grown by more than 20 percent since 1967 (RX's 368H-I, 460; Tr. 909)), and many of these stores–both supermarkets (because wine is more profitable than food) and traditional liquor retailers–are giving more attention and shelf space to wine (Tr. 396, 568, 911–12, 2072, 2108, 2203–04).

152. The tendency of some progressive retailers is, rather than concentrating on a few lines of wines, to offer as wide a variety as possible. Mr. Michael Gelven, the owner of two liquor stores in southeastern Massachusetts, carries the products of more than 100 wine companies, about half of them doemstic (Tr. 2201, 2206–07), because "you want to give the consumer as large a selection as you can. . . ." (Tr. 2210). [47]

153. Mr. Gelven's stores carry a great range of popularly priced wines, including Gallo, Carlo Rossi, Italian Swiss Colony, Paisano, Cribari, Roma, Vino Fino, Ambassador, M. LaMont, California Growers, Setrakian, Vino Casata, Parma, Cappella, Petri, and numerous imports (Tr. 2207–11).

154. Notwithstanding the length of this list, Mr. Gelven takes on three out of four new products offered to him (Tr. 2218–19). He may even seek wines which are not offered by distributors (Tr. 2211). Mr. Gelven searches out new products not only to widen his selection even further, but also because they may be both lower priced for the consumer and more profitable for the retailer (Tr. 2218–20).

155. Mr. Harold Binstein of Gold Standard Liquors is one of the largest retailers in Chicago, with 10 stores serving neighborhoods that are a cross-section of Chicago's diverse population (Tr. 2068–70). He aims to have the largest selection of wines in Chicago, carrying more than 1,000 brands, and he is constantly looking for new wines

(Tr. 2076). At one time or another he has "stocked just about every brand that ever came into the Chicago market." (Tr. 2070). He likes to "have something for everybody" and will ordinarily give all new products a trial in his stores (Tr. 2077–78, 2089), and he has been expanding his shelf space in order to accommodate even more wine. Recently, he opened a 60,000 square-foot store in what used to be a Sears, Roebuck & Co. branch (Tr. 2071–72).

156. At Argonaut Liquors in Denver, second largest of 12 to 15 retailers who together have about 60 percent of the Colorado alcoholic beverage business (Tr. 2106–07), Mr. Jack Robinson stocks about 100 domestic and 150 imported wine brands (Tr. 2108). He is eager to have new products to feed his expanding wine business and also is doubling the amount of available selling space by creating a wine cellar on his store's lower level (Tr. 2108, 2112–13). One of the distributors who services Argonaut Liquors described its attitude, and that of retailers in general: [48]

> If you come in with a new product and you have a presentation, they will buy it. They will at least try it and if there is some movement, they will re-order (Tr. 1970).

157. Wine purchases are to some extent impulse purchases: a wide selection and new products are thus needed to cater to and encourage such impulse buying (Tr. 366, 1454, 2085, 2124). Impulse buyers are drawn to products chiefly by the store's own merchandising–floor stackings, shelf cards, signs, personal contact, and other selling devices (Tr. 2241). Foremost among the retailer's selling devices is low price, which more than any other single factor determines not only the retailer's willingness to take on a product but also his customers' interest in buying it (Tr. 2104, 2112, 2218).

158. As discussed above, retailers seek out products not widely available in order to make their own selections more distinctive and attractive to customers.[18] Products that gain distribution first through key retailers are taken on by other stores as the consumer demand created by the first sellers spreads in the market (Tr. 2220–21). This, in turn, may spur other retailers to seek out additional new products (Tr. 2210, 2218–19).

159. While the vast selection of wines carried by Mr. Gelven is typical only of progressive liquor stores, less innovative retailers and supermarkets may also carry a wide variety of products and brands. In one witness' experience, five or six popularly priced wine brands are typical for a supermarket in the midwest (Tr. 1499–1500)

[18] The owner of Argonaut stated that he likes new competitively priced products because of their uniqueness:
Sure, we like that kind of product because if we can build something on that, on a product that is unknown, we get customers coming back to our store. They cannot go to the next store and find it. . . .They have to come to us. . . . (Tr. 2112).

generally thought to lag behind the rest of the country in wine awareness (Tr. 1571–72). In northern California, Safeway carries 35 [49] different wine brands and other supermarkets may carry 30 (Tr. 902–03, 910–11). Even the non-progressive liquor stores carry more brands than the supermarkets (Tr. 1500).

160. Supermarkets' new interest in wine has made it possible for new wine companies to garner shelf space in them. Bronco is sold in five chains in northern California (Tr. 668–69). California Growers Winery has some chain store distribution in Puerto Rico (Tr. 394). Mirassou Vineyards is carried by seven major chains, which sought its wines, including Safeway in Virginia, California, Washington, and other states (Tr. 2038–39) and Mr. Gary Raden's brand-new line of inexpensive imported Italian varietals has been taken on by Safeway (Tr. 1827–30, 1837–39).

161. Based upon this evidence, I conclude that producers, through existing or new distributors, will be called upon in the future to provide more retail outlets with their wine and that such legal restraints on distribution as there may be will not seriously impede the producers' efforts to sell their wines,

D. Coke-New York's Wine Business

162. Mogen David produces artificially sweetened, predominently kosher specialty fruit and berry wines. These traditional sweet wines account for 40 percent of its sales (CX's 18Z16–17, 19Z1–7; Tr. 1111–14). Founded in Chicago upon the repeal of prohibition in 1933, the company maintains plants there and in Westfield, New York (CX's 12Z7, 18U; Tr. 1108, 1119). The principal markets for these wines are in Illinois, Indiana, Ohio, Michigan, Wisconsin, Florida, Texas and Pennsylvania (CX 12Z5; Tr. 440, 1170). Mogen David sells almost no wine in California and New York, the nation's two leading wine-consuming states, which together account for one-third of the nation's total wine consumption (CX 18Z72; RX 380H; Tr. 1170).

163. Mogen David also produces a specialty wine called MD 20 20 which is Concord based, artificially sweetened and is fortified with alcohol to reach 20 percent alcohol content (CX's 18Z3; 19Z6; 52Z82–83; Tr. 1111, 1114). Mogen David has also produced, at various times, other wines, many of which have been discontinued. [50]

164. Beginning several years before its acquisition by Coke-New York, Mogen David produced a small group of dry kosher wines, including dry Concord, burgundy, champagne, and sauterne (CX 18Z1; CX 19Z6; RX 484C; Tr. 1113–15, 1173). These products failed in the marketplace, however, and never produced any significant sales (Tr. 1113–15, 1172–73). In 1972, they accounted for approximately

one-half of one percent of Mogen David's sales volume (CX 56). As a result, they were dropped shortly after Mogen David was acquired by Coke-New York, before the acquisition of Franzia (CX 58; Tr. 1173).

165. In 1957, Mogen David introduced a line of wines under a new brand name, Key. The line was dropped after a three-year effort to market it failed (CX 18Y-Z, Z33). In 1969, Mogen David introduced MD 20 20, called the "[f]irst major breakaway from [the] Mogen David line" (CX 17U).

166. For a brief period in the early 1970's, Mogen David sold substantial quantities of three other specialty products, each Concord or fruit based and artificially sweetened (Tr. 1172, 1175). Those products were Cold Bear (Concord), Black Bear (blackberry), and Jug (Strawberry and apple) (Tr. 1172, 1175). Cold Bear and Black Bear, after rapid initial success, declined precipitously from a combined sales peak of 1.5 million to 2 million cases per year to less than 70,000 cases per year, with the downward trend continuing (RX's 478, 480; Tr. 126, 1172). Jug declined even more rapidly from its initial burst of 1.2 million cases to its current annual sales of less than 5,000 cases (Tr. 1172).

167. In 1975, several years after discontinuing its previous attempts to market dry wines, Mogen David tried to enter the table wine business by test marketing a dry California table wine produced by Franzia and sold under the brand name Fanfaron (Tr. 1145).[19] The test market results were unfavorable and Fanfaron, like its predecessors, was abandoned as a failure (CX 980K; Tr. 1220). Mogen David sangria also failed in the test market stage (CX 980K; Tr. 1115, 1172). [51]

168. Mogen David has recently renewed its efforts to produce and sell table wines. It has introduced three new wines called Mogen David Light Red, Light White, and Light Pink (CX 1038). These wines, which combine Mogen David wines and sugar solution with wine or grape juice supplied by Franzia, are presently being test marketed in 10 small midwestern and southern cities (Stipulation dated April 18, 1978; CX's 1038, 1040). They are described as "table wines that are lighter and less sweet than the well-known and widely tasted Mogen David Regular Line" (CX 1038).

169. The introduction of new wines has changed the pattern of Mogen David's sales. The sweet traditional kosher wine constituted some 80 percent to 90 percent of Mogen David's business when it was acquired by Coke-New York (Tr. 1114). By 1972, MD 20 20, introduced in 1968, accounted for 50 percent and its Concord wine 19

[19] According to complaint counsel, Mogen David did not try to enter the table wine business because it was already in that business with its sweet wines (CRF, p. 46). I disagree (see Findings 212–237).

percent of total gallon sales volume. The rest of its sales were in fruit and berry wines and other mostly discontinued wines (CX 12Z6). At present, therefore, it appears that some 90 percent of Mogen David's sales are in MD 20 20 and sweet Concord and berry wines.[20]

170. In addition to selling its own products, Mogen David acts as the sales agent for Tribuno vermouth (CX's 12V, 55B). Unlike many other wineries, Mogen David sells no private label wine or bulk wine, and it sells almost no wine to restaurants. Mogen David's share of total wine sold in the United States has decreased in the past several years, as have its actual sales, which declined 33 percent from 1973 to 1977 (CX 992; RX's 416, 417, 418, 425, 501).

Year	*Mogen David & Tribuno Sales (Gallons)*	*Share of Total Wine Sales*
1973	14,289,227	4.12%
1974	11,561,071	3.31%
1975	11,248,754	3.06%
1976	10,490,415	2.78%
1977	9,587,120	2.39%

171. Tribuno is engaged in the production of sweet and dry vermouths of varying alcoholic content and accounts [52] for 23 percent of sales of vermouth produced in the United States (CX 16F) and for 12 percent of all vermouth sales (CX 33F). Until its acquisition by Coke-New York, Tribuno had been a family-owned company in New Jersey bottling and blending vermouth under its trademark in its plant in New Jersey. Some vermouth was also bottled for Tribuno by A. Perelli-Minetti & Sons, Delano, California, from whom Tribuno also purchased bulk wine for its bottling plant in New Jersey. Since the acquisition, Franzia has bottled vermouth for the Tribuno label and has also sold the bulk wine for Tribuno's bottling plant in New Jersey (Tr. 1116-19).

172. Twenty-One Brands distributed Tribuno products from 1941 until its acquisition by Coke-New York (CX 33H). Upon acquiring Tribuno, Coke-New York terminated the relationship with Twenty-One Brands and the Mogen David sales force began to sell Tribuno (CX's 33L, 34, 35; Tr. 1120).

173. Franzia was formally started in 1933 by five Franzia brothers (Tr. 590), although prior to that time, dating back to 1915, the father of the founders of Franzia, Guiseppi Franzia, produced and marketed wine under the Franzia name (CX 91D).

174. In 1933, the company produced 100,000 gallons of wine (CX

[20] This estimate is based on testimony that MD 20 20 sales have been growing only a little (Tr. 1115) and Mr. Sullivan's estimate that at present 40 percent of Mogen David's sales are in traditional sweet (Concord, fruit and berry) wines (Tr. 1112).

91D). In 1962, its capacity rose to 6 million gallons, and by 1973 increased to 36 million gallons (Tr. 592). Franzia underwent a substantial pre-acquisition expansion during the period 1971 through 1973. In 1973, its capital expenditures totalled $5.4 million, and major additions to the plant, equipment and vineyards more than doubled the company's production capacity. Construction of a new $1.3 million bottling facility had previously been completed in 1972, which not only reduced unit bottling costs, but allowed for "considerable future expansion at minimum cost" (CX 5C; Tr. 597–98, 605).

175. Franzia Brothers Winery has one of the most modern wineries in the United States (Tr. 604; CX 5R). It has a storage capacity of 20.3 million gallons and bottling lines with a capacity for 17,000 cases daily (CX's 5R, 75D, 80G). The winery is situated on approximately 100 acres of land near Ripon, California. All of Franzia's wine making operations, general offices and a wine tasting room are located at the winery (CX's 80G, 12Z15). [53]

176. Franzia owns 13 grape producing vineyard properties, consisting of 1,030 acres, within a few miles of the winery. In 1972, Franzia purchased an additional 2,500 acres of undeveloped agricultural property located approximately four miles from the winery. The company also entered into 35-year leases on 2,384 acres in 1972, with 13 lessees (CX's 75D, 80G; Tr. 603).

177. In 1972, vineyards owned and operated by Franzia supplied approximately 7 percent of all grapes crushed. The balance of Franzia's annual grape requirements has been supplied by more than 200 independent growers. A large number of these growers have been selling their grapes to Franzia for many years. The vineyards purchased in 1972 were expected to begin producing grapes by 1975 (CX 12Z14).

178. Franzia produces and markets a broad line of varietal and generic still, sparkling, dessert, vermouth and pop wines (CX's 12Z13, 80C, 532; Tr. 598, 1035). At the time of the acquisition of Franzia by Coke-New York, it was producing and marketing the following wines:

Red Table Wine

Zinfandel, Burgundy, Vino Rosso, Robust Burgundy, Chianti;

White Table Wine

Chablis, Sauterne, Rhinewein, Chablis Blanc;

Rose Table Wine

Vin Rose, Grenache Rose, Pink Chablis;

Sparkling Wine

Champagne, Pink Champagne, Cold Duck, Sparkling Burgundy;

Dessert Wines

Straight Sherry, Port, Tawny Port, Pale Dry Sherry, Very Dry Sherry, Cream Sherry, Tokay, Muscatel, White Port; [54]

Vermouth

Dry Vermouth, Sweet Vermouth. (CX's 12H, Z13, 75G, 80C; Tr. 597–98).

179. Franzia never produced berry wines, although it is capable of doing so (Tr. 600), and has also experimented with specialty wines called Davance, Liberte, and Silver Hawk (Tr. 1034–35).

180. Franzia also makes and sells bulk wine to other wineries, including Gallo, Sebastiani and Sonoma Vineyards (Tr. 897), sells grape concentrate[21] to Mogen David (CX's 565A–B, 1041B; Tr. 778–79, 1150), and has purchased apple concentrate from Mogen David (CX 843).

181. From 1971 to the time of the acquisition of Franzia by respondent Coke-New York, Franzia was a profitable company (CX 12X; Tr. 1781, 1808). In 1972, the year prior to the acquisition, Franzia's sales and revenues had increased 32 percent over 1971 while earnings rose 58 percent. Sales in 1972 were $21,439,000 while earnings were $859,000 (CX 75D). By 1973 sales had increased to $28,931,000 (CX 12X). The company's assets as of June 1973 totalled $20,529,000, an increase of over $5,000,000 from 1972 (CX 12Z32). During the period 1970–1973, Franzia's California sales increased by 50 percent, while its non-California sales more than doubled (CX 886). Non-California sales rose 37 percent in 1972 alone (CX 75D).

182. On a gallonage basis, Franzia's yearly sales increased 12.8 percent in 1969; 12.1 percent in 1970, 14.5 percent in 1971; 17.9 percent in 1972 and 32.4 percent in 1973. Each increase is measured against the preceding year's sales (CX 12Z12).

183. Respondent Coke-New York was aware of Franzia's financial condition when the company was acquired. The accounting firm of Ernst & Ernst was utilized by respondent to report to them on Franzia's financial condition (Tr. 1810–11). [55]

184. Franzia's rapid growth just prior to the acquisition was

[21] Dehydrated grape juice (Tr. 29–30).

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caused by a tremendous spurt in the demand for California wines in the early 1970's and a short grape crop in 1972 (RX 378F; Tr. 1801). During this time, Franzia also experienced a capital shortage which arose from the unwillingness of three of the Franzia brothers to finance expansion (Tr. 598). Eventually, these brothers sold their 60 percent interest in Franzia to a group headed by investment banker Daniel Lufkin (Tr. 590, 597–98, 1186).

185. The quest for additional capital to finance Franzia's expansion led to a public offering of Franzia stock by the Lufkin group early in 1972 (Tr. 1807). Franzia also obtained large loans from the Wells Fargo Bank in 1971 (Tr. 1187, 1807). The additional capital—both equity and debt—was invested in expansion of the winery (CX 12Z14–15; Tr. 597–98).

186. At that time, the early 1970's, Franzia's business was growing (Tr. 1781). More capital was needed to finance the planned expansion. Franzia was, however, already fully borrowed and the banks required equity capital as a prerequisite to more additional loans (Tr. 1188, 1209, 1807). Therefore, in April 1973, Franzia attempted a second public offering of its stock. Adverse conditions in the stock market made the offering unsaleable and it was withdrawn (CX 77C; Tr. 1188, 1781).

187. The Lufkin group then contacted Coke-New York, which had expressed an interest in Franzia previously, and a sale of the Lufkin group's interest together with that of the two remaining Franzia brothers was arranged; the sale was closed on December 14, 1973 (CX 50; Tr. 1186–91). Franzia was acquired for approximately $40 million worth of Coke-New York stock (Tr. 1150).

188. When Coke-New York acquired Franzia, Franzia's large bank debt was paid off by Coke-New York and replaced by an equivalent inter-company debt (Tr. 1208–09). Franzia pays interest to Coke-New York at the prime rate, a rate lower than Franzia could otherwise obtain and lower than the "prime plus" paid by Coke-New York on the money it borrowed to pay off Franzia's debt (RX 388A-Z17; Tr. 1209). Additional funds were also advanced to Franzia by Coke-New York to finance the completion of improvements in the winery and to cover the operating **[56]** losses Franzia sustained beginning in 1974. Coke-New York's role as Franzia's banker brought Franzia's total debt to Coke-New York to $27.6 million as of September 30, 1976 (RX 388A).

189. For reasons which are not clear in the record, from the date of the acquisition through the end of 1977, Franzia suffered losses totaling approximately $11.6 million: $2.5 million in 1974, $4 million in 1975, $2.9 million in 1976, and $2.2 million in 1977 (RX 338; Tr.

1208). In 1975, Coke-New York concluded that Franzia would never yield an acceptable return on investment and attempted, unsuccessfully, to sell the company (Tr. 1211–15). In addition to its own efforts to sell Franzia, Coke-New York retained the investment banking firm of Blyth Eastman Dillon & Co. Inc. to attempt to find a buyer. Although working for a large contingent fee, the investment bankers were also unable to find a buyer (Tr. 1214–15). Indeed, neither Coke-New York nor the investment bankers were able to generate any bids for Franzia at any price (Tr. 1211–15).

190. In the course of these efforts to sell Franzia, discussions were held with, among others, six large companies: PepsiCo, Inc., The Coca-Cola Company, Norton Simon, Inc., Gulf & Western Industries, Inc., Continental Grain Co., and Northwest Industries, Inc. Price was never discussed with any of the six companies because none of them was sufficiently interested in Franzia even to inquire about the price[22] (Tr. 1213–14). [57]

191. Norton Simon's former acquisition manager, John Anderson, explained that Norton Simon had rejected Franzia because "it had no major established brand, and it was private label oriented." It was, he said, "a 'dog'." (Tr. 1764). The Coca-Cola Company rejected Franzia because it concluded that Franzia's business had inadequate margins and that Franzia could not be shifted from its operation into a more profitable wine business (Tr. 1214).

192. In addition to its heavy losses, Franzia has also suffered a sales decline over the past five years, both in gallons and as a percentage of total United States wine sales (CX 992; RX's 406, 418, 425, 501).

Year	*Franzia Sales (Gallons)*	*Share of Total Wine Sales*
1973	10,602,453	3.05%
1974	10,518,572	3.01%
1975	10,621,860	2.89%
1976	11,077,310	2.94%
1977	9,294,287	2.32%

193. Franzia's heavy losses have also had substantial adverse effects on Coke-New York (Tr. 1210–11). The high price paid for Franzia, combined with its poor performance in the face of competition, assures Coke-New York of an extremely large loss in the event

[22] These companies were and are interested in the wine business, notwithstanding their lack of interest in Franzia. Some were owners of or have subsequently acquired wine businesses. PepsiCo, Inc. owns Monsieur Henri Wines, Ltd. (RX 13K). The Coca-Cola Company subsequently acquired The Taylor Wine Company, Inc. (RX 3H). Norton Simon, Inc. acquired Somerset Wine Company (RX 12Z9). Northwest Industries, Inc. acquired Buckingham Corporation, the importer of Cutty Sark Scotch and wines (CX 11H, O).

of a sale of Franzia, if indeed it can be sold (Tr. 1216). This state of affairs, which Coke-New York has had to disclose to investors, has caused the company's auditors to question the value of the investment in Franzia and to qualify Coke-New York's financial statements (Tr. 1215). Dissolution of Franzia and piecemeal sale of its assets—likely to be the only practicable method of sale—are still likely to produce a huge loss for Coke-New York, which has an annual net income of only about $10 million (Tr. 1210, 1216–17). Although it is difficult to assess the precise impact of Franzia's losses on Coke-New York's stock, the fact is that it has declined substantially, from about $25 at the time of the acquisition to $3 5/8 afterwards, later creeping back up to just over $9 (Tr. 1211, 1215). [58]

E. The Relevant Markets

(1) The Relevant Geographic Market

194. The parties agree that the relevant geographic market in which the effects of Coke-New York's acquisition of Mogen David are to be measured is the United States as a whole (complaint counsel's response to interrogatories, January 9, 1975 at 2).

(2) The Relevant Product Market

195. One of the alleged effects of the challenged acquisition is the elimination of competition between Coke-New York and Franzia. Coke-New York, through Tribuno and Mogen David, did produce some wines prior to the acquisition which were similar to wines produced by Franzia, but these were a minor aspect of Coke-New York's business.

196. Complaint counsel, faced with the fact that Coke-New York and Franzia produced totally different wines prior to the acquisition, argue that these companies nevertheless competed because "wine is wine."

197. At first blush, this proposition seems unsupportable, for Tribuno, located in the eastern United States, produced only vermouth (Finding 171) and Mogen David, located in the East and Midwest was most well-known for its line of sweetened wines (Findings 162–163), whereas Franzia was a typical producer of popularly priced California table, dessert and sparkling wines (Finding 178).

198. However, complaint counsel's claims cannot be that easily dismissed, for the record reveals that the average wine drinker is willing to experiment. He does not limit his custom to a particular

wine producer or to any single type of wine, so that one can say that, despite distinct differences in color and taste, a white chablis may, when one is selecting a dinner wine, be considered along with many other red, white and rosé table wines selling at the same, and perhaps higher or lower prices. [59]

199. On the other hand, one cannot ignore the fact that the manhattan and martini drinker uses only vermouth when he mixes his drinks. The availability of other wines is a matter of complete indifference to him.

200. Whether there is an "all wine" market, as argued by complaint counsel, is clearly a difficult question. I have considered the following facts in testing the validity of their contention:

(a) Mogen David's Perception of Its Place in the Wine Industry

201. Complaint counsel argue that Mogen David views itself as being part of the wine industry, citing a response from Coke-New York's counsel to an FTC letter of inquiry in which it was conceded that Mogen David's Catawba, Rosé, Dry Red, dry Concord, Burgundy and Sauternes competed or attempted to compete with other producers' table wines (CX 58A-B). Complaint counsel also point to instances in which Mogen David compared its position with other wine producers, either singly (CX 564) or in the aggregate (CX's 23A-D, 24N, 748, 749).

202. Mogen David also attempted to play down its Concord wine image in an advertisement which emphasized its line of wines:

> If Mogen David makes you think of Grandma and Concord wine. . .think again! Think variety!. . .Mogen David is a full line of wines. Generics, varietals, and sparkling wines. . .In fact, Mogen David has become the sixth largest domestic producer and marketer of advertised branded wines. . .and we're still growing. . .Mogen David. . .the growth company in the wine industry (CX 971).

203. The marketing reports filed by the Mogen David field representatives, also relied upon by complaint counsel, contain information on "competitors" and show that it follows the activities of many wineries. For example, before the acquisition of Franzia, a Mogen David sales representative referred to Franzia as "competition." (CX's 306, 332, 333). [60]

204. Mogen David salesmen follow and report on California premium wineries (CX's 123, 143, 145, 211, 253B, 272B, 288B, 299, 310, 321, 374, 459, 477), imported wines (CX's 140, 143, 145, 154, 168, 175, 295B, 308, 424, 503) and California popular priced wines (CX's 116, 134, 135A, 136, 143, 145, 163, 168, 169A, 211, 255, 264B, 266B, 269,

296B, 306, 310, 317, 321, 333, 341B, 352C, 353B, 357B, 361, 370, 377, 382, 389, 441B, 454, 461, 466, 479).

205. Both before and since the Franzia acquisition, Mogen David has paid some attention to the prices charged by Gallo and United Vintners (CX's 266A-B, 269, 289B, 310, 454, 466, 813; RX 121).

206. Even before the Franzia acquisition, Mogen David field personnel paid some attention to the prices charged by Guild (CX 264B), Gallo Chablis Blanc (CX 266B), California wines generally (CX 299), Gallo, Christian Brothers, Paul Masson and Almaden (CX's 310, 477), Gallo table and dessert wines (CX 454), Italian Swiss table and dessert wines, Roma table and dessert wines (CX 454), and Gallo champagne (CX 466).

207. Mogen David follows the activities of other wineries. For example, the company was apparently interested in the prices of California wines after the acquisition (Tr. 808), it collected advertising expenditures figures of all firms in the industry, referred to as the "competition" (CX 544E–F; see also CX's 686A–R, 694A–Y, 692A–G) and collected consumption figures of all wine in an effort to determine its advertising budget (CX 544K; see also CX 24Z9).

208. The significance of Mogen David's tracking the activities of California or imported table wines has, however, been overemphasized by complaint counsel, for its salesmen, in some of the reports which complaint counsel cite, also discuss the activities of spirit producers (CX's 116, 123, 140, 143, 145, 168A, 175, 288, 295). Nor is it surprising that Mogen David would be interested in California wines after the acquisition of Franzia for that company's wines are similar to those wines. And, comparisons of Mogen David specialty wine prices with those of California producers prove nothing **[61]** about competition between Mogen David's kosher wines, MD 20 20 and California table wines. For example, see CX 813L which compared Mogen David's "Jug" prices with Gallo's Boone's Farm wine, neither of which are table wines. Furthermore, while Mogen David's management and employees may have believed or tried to convince others that it was a member of the table wine industry, evidence presented by other industry members indicates that this perception was not accurate insofar as Mogen David's heavily sweetened kosher wines and its other major product, the specialty wine, MD 20 20, are concerned.

(b) Consumer Perception of Mogen David Wines

209. In 1970, Creative Research Associates, Inc., at the request of Mogen David, conducted a study (CX 737A–Z85) to determine the position of Mogen David in the wine market in order to facilitate a

highly directed marketing plan for its current and future products (CX's 731B, 737I–J). The proposal for the study suggested that it should obtain information on the current user of Mogen David wine, the perceived role of Mogen David among other wines and alcoholic beverages and the overall elasticity of the Mogen David name (CX 731B). Complaint counsel claim that this study reveals consumer attitudes toward Mogen David wines and supports their claim that those wines compete with other wines.

210. In my opinion, the study cannot be used for the purpose for which it was offered, for its author agreed that it was not intended to and did not give a statistically accurate picture of wine purchasing behavior even in the four cities in which interviews were conducted (Tr. 1613). Coke-New York also points out what appear to be serious problems with the study's conclusions as to the attitudes of those who were interviewed (RRF, pp. 26–29), but since the study cannot, in any event, form a basis for any conclusion about competition between Mogen David and other wines, there is no need to analyze its methodology. The same is [62] true of the Edward H. Weiss study, whose author was not called by complaint counsel (CX 52A–Z165).[23]

211. A more reliable indicator of consumer attitudes toward Mogen David wines is, in my opinion, the testimony of wine producers and retailers who base their business decisions on their customers' desires. If their customers perceived that Mogen David wines[24] tasted like and could be used for the same purposes as other wines, one would expect that, over the years, producers would have concluded that Mogen David was a competitor. That has not happened, however.

(c) Industry Perception of Mogen David Wines

212. Some witnesses made the broad statement that all wines compete. Mr. Perelli-Minetti of CWA stated that "the consumers buy all types of alcoholic beverages, and I think we all compete with each other" (Tr. 108). [63] However, his opinion was contradicted by Mr. Robert Arnold, who is actually in charge of CWA's sales and marketing (Tr. 457–58). He said that CWA and Mogen David are not

[23] Compare *Bristol-Myers Co.*, 85 F.T.C. 741 (1975):

> The Commission has on numerous occasions considered the question of the admissibility of surveys which are obviously hearsay, and it is well settled that such surveys will be admitted for the truth of the matters asserted when it is demonstrated that they are reasonably reliable and probative. *Id.* at 743–44.

Although these studies were admitted in evidence to show the attitudes of the individuals who were surveyed, they are not "reliable and probative" with respect to the attitudes of a significant segment of the population.

[24] According to complaint counsel, the meaning of "Mogen David wines" is unclear because Mogen David produces many wines (CRF, p. 49). However, most of its wines are heavily sweetened Concord or berry wines, industry members are aware of this, and clearly were referring to these kinds of wine when they were questioned about competition with Mogen David.

competitors and that Mogen David drinkers would not be likely to drink California wines (Tr. 460–61). Furthermore, when Mr. Perelli-Minetti was asked to identify various wines with which he was familiar, being told specifically not to limit his answer to California, he did not mention Mogen David or Manischewitz (Tr. 64–66). This reveals, much more than does his general statement, the lack of significant competition between CWA's wines and Mogen David's wines.

213. Although Meyer Robinson, general manager of Manischewitz, purports to "look at the whole picture," he regards Manischewitz' traditional products' "competition as being made up of Mogen David and Carmel and Kedem, depending on the market." (Tr. 1457).

> In some markets, it is Manischewitz and all the rest combined and in some markets it depends on the market - it is Manischewitz and Mogen David. In some markets it is Manischewitz and Carmel. In others it is Manischewitz and Kedem. (Tr. 1457–58).

214. Angelo Fantozzi, who distributes CWA's wines in Chicago, professed to view all wines as generally in competition, but conceded that he pays far less attention to Mogen David's prices than he does to the prices of products "corresponding" to the ones he distributes (Tr. 1513, 1521–22). Under cross-examination, Mr. Fantozzi admitted that the day before he testified he might have said he did not follow Mogen David's prices at all (Tr. 1520–21), and I believe that his testimony on direct is, therefore, not credible.

215. Mr. John Simon of Bardenheier was "included to think that every wine is in competition with every other wine," at least, those "priced roughly in our category." (Tr. 1577). [64]

216. Other producers do not view Mogen David as a competitor.[25] East-Side Winery's general manager Ernest Haas testified that East-Side pays no attention to any of the Mogen David products, does not share consumers with Mogen David, and is not in competition with Mogen David.

> JUDGE PARKER: Mr. Haas, are you familiar with Mogen David wine?
> THE WITNESS: Yes.
> JUDGE PARKER: What category does that fall into?
> THE WITNESS: I—
> JUDGE PARKER: (Interposing) Pop wine?
> THE WITNESS: It's in a category all by itself as far as I'm concerned. Wines of that sort, the kosher wines or berry wines, they are in a category all by themselves. (Tr. 238).

217. Mr. Fred Weibel, chief executive of the winery that bears his

[25] Complaint counsel argue that Coke-New York's attorneys asked producers who their "principal" competitors were (CRF, p. 4), hinting that if the proper question had been asked, Mogen David might have been named as a "secondary" competitor. Of course, complaint counsel could have rectified this alleged deficiency on redirect.

family name, testified that neither his products nor those of Franzia compete with any Mogen David product (Tr. 308, 324-25). Mr. Setrakian, the president of California Growers Winery, said that theoretically all wines compete (and perhaps all alcoholic beverages), but that he isn't worried about the prices of somebody's Concord cream (Tr. 390-91). Gibson's general manager, Mr. Marvin Jones, stated that the people who [65] drink Gibson's conventional[26] wines do not drink Mogen David's (or Gibson's Mogen David-type) products (Tr. 523-26).

218. While Robert Ivie, president of Guild and former chairman of the California Wine Institute, believes that almost all wine producers compete keenly with each other, he does not believe that Guild's broad line of conventional California products competes with Mogen David (Tr. 581). In response to complaint counsel's question, he testified:

> I would say, to go further, I don't think that you could say that the same consumer that is going out today to buy a bottle of Cribari is one that is going to buy a bottle of Mogen David this afternoon. (Tr. 583).

Cribari is one of Guild's brands of popularly priced wines that Mr. Ivie identified as directly competitive with Franzia (Tr. 539-40, 580-81).

219. Calling Mogen David and Franzia products "as different as night and day," Joseph S. Franzia of Bronco stated unequivocally that the customers for his company are different from the customers for Mogen David products (Tr. 679-80). Nor does Sonoma Vineyards share consumers with Mogen David, although it does with Franzia (Tr. 1767-68). According to Mr. DePompei, Mogen David drinkers do not buy Franzia generic and varietal wines (Tr. 1338-39).

220. In addition to these witnesses, all of whom were called by complaint counsel, other producers of conventional wines at all price levels testified that while they share customers with each other and with Franzia, they do not share them with Mogen David (Tr. 1914-15, 2036-37). Some [66] witnesses recognized that consumers of conventional wines are likely to purchase different price wines for different occasions (such as everyday drinking and entertaining) but doubted that the diversified buying habits of conventional wine drinkers extended to Mogen David (Tr. 1767-68, 2082-83, 2116).

221. Evidence of consumer attitudes toward Mogen David was also presented by three retailers called by counsel for Coke-New York. Mr. Harold Binstein of Gold Standard Liquors operates 10

[26] Despite complaint counsel's claim that the term "conventional wine" is argumentative (CRF, p. 50), there is so much evidence of the differences between Mogen David's wines and other wines that the term is an apt description of those other wines.

stores scattered throughout the Chicago metropolitan area; Mr. Jack Robinson of Argonaut Liquors operates a single large store in Denver, serving customers from throughout Denver, the state, and the region; Mr. Michael Gelven of Big D Liquors operates two stores in rural southeastern Massachusetts (Tr. 2070–71, 2103, 2109–10, 2225–29). All three retailers, who own a total of 13 stores, had observed the buying patterns in their stores over a considerable period of time and had observed that Mogen David wines are purchased by a group of people who "are not really wine drinkers" (Tr. 2228–29), and that Mogen David drinkers and other wine drinkers "are two distinctive types of customers" (Tr. 2082–83, 2116–17).

222. Mr. Harold Gomberg, a wine consultant, stated in a report to Mogen David, that those who refuse to recognize its wines as "real" wines are "snobs" (CX 18Z11–12). This harsh appraisal is, I believe, incorrect for it is clear that most of Mogen David's wines[27] are quite different from conventional wines.

(d) Differences Between Mogen David Wines and Other Wines

223. Mr. Arnold of CWA described Mogen David as a maker of "sharply different" products with a "Concord base" and as being essentially like a "grape juice," and stated that "we are not in that business" [67] (Tr. 460–61, 473). Mr. Weibel disparaged the Mogen David product with a rather earthy word (Tr. 311), and described its taste as "foxy" (Tr. 279). Other witnesses described Mogen David wines as "considerably sweeter" than other wines and "syrupy."[28] Even the sweetest conventional wines are not comparable in taste to Mogen David wines (Tr. 522–23, 311, 2271). Mr. Haas, of East-Side Winery, concluded that Mogen David wine is "in a category all by itself as far as I'm concerned. Wines of that sort, the kosher wines or berry wines, they are in a category all by themselves" (Tr. 238).

224. One retailer stated that MD 20 20, Mogen David's biggest seller, is, like its traditional wines, different from table wines:

> . . .I class it and this is my personal classification, as in the class with the beverage type wines, the apple types, the Boone's Farm, which is a category that is basically on its way down. It was high a few years ago when the cold duck was big, in that area. It seems to have lost a lot of its appeal now. It is usually sort of an area of its own, usually young people (Tr. 2271).

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[27] The exception would be the light table wines recently introduced by Mogen David (Finding 168).

[28] The Mogen David Concord wine is, in fact, very sweet. It contains 18 percent to 19 percent sugar (Tr. 523). In comparison, Gibson's sweetest California-produced wines contain 8 percent sugar, cream sherry contains approximately 6 percent to 7.5 percent sugar and dry table wines close to 0 percent sugar (Tr. 269, 523, 530).

These conclusions as to the basic difference between Mogen David wines and other wines are supported by the fact that one recent crisis in the raw material market affected Franzia (and other table wine producers) but not Mogen David, and another affected Mogen David, but not Franzia. The California wine glut of 1974 did not hurt Mogen David's prices at all (Tr. 1260–61); conversely, the sharp rise in the price of sugar in 1973 and 1974 forced Mogen David's cost and prices upward but had no impact whatever on Franzia (RX's 59E, 328Y; Tr. 1260–61). [68]

225. Industry opinion about Mogen David's wines was echoed by Mr. Louis R. Gomberg, a wine industry consultant, who wrote a report on Mogen David for Coke-New York which concluded that Mogen David "has no real competition in the markets it dominates. Perhaps. . . because it combines distinctive taste with a distinctive brand/type name." He went on to say:

> One thing is certain: Mogen David Concord Grape Wine is unique. With only one competitor in its field (Manischewitz), the competition is somewhat remote as Manischewitz has strength in only a few markets and its sales volume is estimated at only about one half to two thirds that of Mogen David. . . . It is not really a table wine in the traditional sense, although generally so classified, nor is it an appetizer or dessert wine, although sweet enough to qualify for the latter grouping. (CX 18Z40).

Mr. Gomberg also suggested in this report that the Mogen David brand placed its wine line in a different category than other wines:

> It could very well be that Mogen David, either as a brand/type name or simply as a brand name, is inescapably identified with the image or images the name now evokes and that no amount of persuasion, no matter how well planned or heavily financed, is apt to convert non-users to users. (CX 18Z16).

226. Another indication that Mogen David is in a different business than the producers of California wines appears in the testimony of Mr. Sands, president of Canandaigua Wine Company, a New York State winery. Even though Canandaigua produces a line of table wines which are much closer to California table wines than are Mogen David's traditional wines,[29] it purchased a California [69] winery because it "wanted to get into the California wine industry." (Tr. 1374).

227. Another difference between Mogen David and most other wines is that they are produced in different areas of the country (Finding 162) and, apparently because of this Coke-New York did consider producing Mogen David products at the Franzia winery in California (Tr. 1178–79). However, when it became clear to Coke-

[29] Canandaigua produces New York State table wine, fortified wines, sweet wines and sparkling wines (Tr. 1343).

New York that its principal products could not legally be made in California (Finding 38), it experimented with making MD 20 20 by using grape concentrate (whose use is legal in California) instead of cane sugar as a sweetener. However, Mr. Sullivan, executive vice president of Coke-New York, testified that he vetoed putting the experimental MD 20 20 into production because the taste was off and it was not the same product (Tr. 1258).[30]

228. Mogen David was so little thought of as a competitor by the wine industry or as an acquisition candidate that Mr. Gomberg felt it necessary to explain the reasons to the management of Coke-New York:

1. Most winery acquisition interest has been focused on California properties, with little or no thought given to [70] wineries located elsewhere, except New York State, because California is the focal point of wine action in the U.S. All else is peripheral.
2. Mogen David is seldom mentioned in wine reports of any kind–consumption, travel, investment, agriculture, etc. Consequently, few ever think of it as a part of the U.S. wine industry.
3. California wine gets practically all of the U.S. wine publicity. Even the New York (Finger Lakes) area receives scant notice. Illinois, virtually nothing. To that extent, then, Mogen David doesn't exist.
4. The image of Mogen David often tends to be thought of as ethnic even though this is true only to a limited degree and then only as far as markets are concerned. The investment fraternity thus is inclined to regard Mogen David as unsuitable—for the same reason that Monarch Wine Company (Manischewitz) probably is so regarded.
5. Mogen David actually was sold not too many years ago. Some who otherwise might think of it as a candidate for acquisition therefore may subconsciously dismiss it as unavailable at this time, because of the knowledge of its earlier sale. (CX 18Z70–71)

(e) Comparison of Wine Prices

229. Since wine is so price-competitive (Findings 67–77), wine producers carefully watch their competitors' prices and take them into account when setting their prices (Tr. 250, 308, 390–92, 580–83, 1768, 2286–88). [71] These price comparisons do not, however, take Mogen David wines into account, a very convincing indication that they do not compete with most other wines.

230. Mr. Ivie, of Guild, evaluates the prices of competitors of each of its brands (Tr. 583). In naming his "pricing keys" (or competitors),

[30] According to Mr. Gomberg, Gallo and Roma also experienced the same problem (CX 18Z40–41). As to Gallo: Gallo tried to make a niche for himself in the California market with a product roughly resembling Mogen David, called *Galloette*. It too, bombed after a few years although supported by a powerful consumer-sampling campaign in the San Francisco market. Probable reason for its failure: a caramel-like off-flavor derived from the grape concentrate used for sweetening; relatively obscure on the first taste but all too unpleasantly prominent on subsequent tastes. (California regulations prohibit the use of grape wine sold as such). (CX 18Z41).

Mr. Ivie did not list Mogen David or Manischewitz (Tr. 580). East-Side Winery pays no attention to Mogen David prices (Tr. 250). Sebastiani, which sells premium wines, and watches the prices of such competitors as Mirassou, Beringer, Krug, Almaden and Paul Masson, has no idea of what the prices of Mogen David wines are (Tr. 2286-88). Other producers expressed no interest in Mogen David's prices (Tr. 308, 390-92, 1768).

231. Conversely, neither Mogen David nor Manischewitz review the prices of popularly priced California wines (Tr. 1171-72, 1467-70). Mr. Meyer Robinson, Manischewitz' general manager, stated that he would be concerned if Mogen David's wines were 25 or 50 cents a bottle cheaper than Manischewitz, but that he would not be bothered if Franzia wines sold below his wine (Tr. 1470).

232. Generally, the Mogen David-type wines sell for more than popularly priced table wines. In California, Manischewitz' prices were almost twice Franzia's-more than $1 a bottle in some cases (RX's 423, 424). Gibson Wine Company is the largest California producer of fruit and berry wines and also produces conventional wines (Tr. 521-22). Gibson treats these wine categories differently, in one advertisement calling its fruit and berry wines "old fashioned" (CX 966; see also CX's 967, 968, 969, 970). Gibson also prices its fruit and berry wines differently. They are twice the price of the conventional table wines and nearly that much higher than the conventional dessert wines (RX's 135, 136A-B, 146, 147, 148, 155, 160).

(f) Shifts in Wine Consumption

233. In the 1950's and 1960's, dessert wines were more popular than table wines. Today, the reverse is true (Tr. 52-53, 1322): "There has been a strong [72] trend away from dessert wines to dry table wines" (Tr. 366). At one time, red table wine was more popular than whi . White now enjoys more favor in the consumer's eyes than red (Tr. 387). Pop wines, which had tremendous growth in the late 1960's and early 1970's, are much less popular now (CX 271; Tr. 53). Cold Duck, once so popular, is fading (Tr. 1553), whereas sparkling wines and champagne are finding increased sales (Tr. 53). There is some evidence that slightly sweeter table wir s, at least among less sophisticated wine drinkers, are more popular than dry table wines (Tr. 529) although this opinion is challenged by other industry members (Tr. 366).

234. These changing consumption patterns are due to the penchant of the wine drinker to sample a wide variety of wines (CX

52Z152; Tr. 55-56, 230, 503, 574-75, 600, 1370), frequently on impulse (Tr. 1453-54, 1499, 1571-72, 2124, 2241).

235. The infrequent or beginning drinker prefers wine with some sweetness rather than one that is perfectly dry (CX 27Z290; Tr. 55). The sweet wine that introduces a consumer to wine may be Mogen David (Tr. 472-73, 1407-08, 1504, 2289, 2301-02), Manischewitz (Tr. 472-73, 1407-08, 1459, 1503-04), a pop wine (Tr. 2301, 2237), Cold Duck (Tr. 237, 1553), Sangria (Tr. 1503-04), a sweet German or Italian wine (Tr. 1503-04), or other very sweet or mildly sweet wines (Tr. 1407-08). The exceptions, those who begin their wine adventure with dry wines, tend to come from an ethnic origin where dry wines are habitually consumed (Tr. 1370).

236. Consumers' wine habits reveal that one cannot view competition too narrowly. A chablis undoubtedly competes not only with other white still table wines but also with red table wines and, as far as other consumers might be concerned, at particular times, even with champagnes or other sparkling wines.

237. Shifting preferences in wine do not, however, prove that there is an "all wine" market, for one must also consider that there is an apparent trend to substitution of wines for spirits. Messrs. Perelli-Minetti, Setrakian and Sebastiani apparently perceive distilled [73] spirits and beverages as fringe competitors (Tr. 57, 390-91, 2287, 2297). The importers of Cutty Sark believe that the cross-over from scotch to wines and other spirits hurts its sales (RX 110), and pop wine drinkers of the early 1970's are thought to have shifted to beer (Tr. 1239). If one were to accept complaint counsel's argument that the obvious differences between Mogen David and conventional wines should be ignored in favor of an "all wine" market, one might, in light of the evidence of wine's apparent inroads into the liquor and beer business, just as easily ignore the obvious differences between these products and find an "all alcoholic beverage" market.

F. Market Data

(2) Coke-New York's Share of the "All Wine" Market Alleged by Complaint Counsel

238. Coke's first acquisition, Mogen David, increased its market share[31] and market rank each year for the years 1969 to 1973. It ranked ninth among wine producers in 1969, eighth in 1970, sixth in 1971, fifth in 1972 and (counting Tribuno but not counting Franzia) fourth in 1973. Its market share increased from 1.89 percent in 1969

[31] Market share data is stated in gallons and the universe includes taxable withdrawals of U.S. produced wines and imports for consumption of foreign wine (CX 991A-C).

to 2.29 percent in 1970, to 2.77 percent in 1971, to 3.49 percent in 1972, and to 4.12 percent (counting Tribuno but not counting Franzia) in 1973 (CX's 991A-C, 992, 996).

239. Franzia increased its market share each year from 1971 to 1973, and ranked sixth or seventh among wine producers each year from 1969 to 1973. In 1971, its market share was 2.38 percent; this increased to 2.68 percent in 1972 and to 3.05 percent in 1973 (CX's 991A-C, 992, 996).

240. Through its ownership of Mogen David, Coke-New York had a market share of 3.49 percent in 1972. In 1973, after acquiring Tribuno and Franzia, its market share was 7.17 percent. Without the Franzia acquisition, Coke-New York's market share would have been 4.12 percent. The difference in market share of Coke-New York with and without the Franzia acquisition was 3.05 percent in 1973 (CX 992). [74]

241. After the Franzia acquisition in 1973, Coke-New York became the third largest wine producer; without the acquisition it would have ranked foruth (CX's 991, 992). In 1973, the market shares of the top four wine producers were:

Gallo	28.38%
Heublein, Inc.	15.63%
Coke-New York	7.17%
National Distillers	4.39%
Total	55.57%

(CX 992)

242. Since 1974, the total market share of the top four wine producers has declined:

	PERCENT OF TOTAL SHIPMENTS			
COMPANY	*1977*	*1976*	*1975*	*1974*
Gallo	*	26.89%	26.95%	28.33%
Heublein/United Vintners	*	15.65%	17.46%	16.57%
Coke-New York	4.72%	5.73%	5.95%	6.35%
National Distillers/Almaden	*	5.10%	4.59%	4.52%
Total	*	53.37%	54.95%	55.77%

* Information not available.

(RX's 418B, 425, 501)

(2) Concentration in the "All Wine" Market

243. The four and eight firm concentration ratios in the wine industry for the years 1968-73 were:

	1968	*1969*	*1970*	*1971*	*1972*	*1973*[32]	*1973*[33]
Four Firm	46.93	49.81	52.70	56.21	54.31	52.52	55.57
Eight Firm	56.17	59.18	62.50	66.31	65.55	64.56	66.72

(CX 993)

[75] 244. Coke-New York's acquisition of Franzia resulted in a change of four and eight firm concentration ratios. The four firm ratio was 3.05 percent greater with the merger than without it. The eight firm ratio was 2.16 percent greater. From 1968-73 the eight firm concentration ratio (not including the acquisition) rose 8.39 percent.

245. This picture has changed in recent years. From 1974-76, the combined market share of the four largest producers dropped 2.40 percent (from 55.77 percent to 53.37 percent). Four firm concentration in 1976 was 0.67 percent higher than in 1970. The largest winery, Gallo, as well as Heublein and Coke-New York have recently been losing market share to the smaller wineries. Gallo's share of total wine sales declined from 32.66 percent in 1971 to 26.89 percent in 1976 and was lower in 1976 than it had been at any time since 1969. Heublein's sales, although not consistently declining, slipped from 17.85 percent in 1969 to 15.65 percent in 1976. From 1974 (the first post-acquisition year) to 1977, Coke-New York's share of total wine sales fell from 6.35 percent to 4.72 percent. Of the largest four firms, only the fourth (National Distillers/Almaden) increased its share of sales, rising steadily from 2.32 percent in 1968 to 5.10 percent in 1976 (CX 992; RX's 418B, 425, 501).

G. Coke-New York's Plans for Franzia and Post-Acquisition Changes in Franzia's Business

(1) Plans

246. Prior to its acquisition, Coke-New York planned to make Franzia management personnel responsible to Mogen David officials (CX's 680F-G, 718D). A preacquisition document prepared in the fall of 1973 (CX 718B) made the following recommendations:

A. Merchandise Franzia in existing markets through Mogen David as soon as possible.

B. Simultaneously test upgrade image including:

[32] Reflecting Franzia and Coke-New York as separate firms.

[33] Reflecting Franzia and Coke as a single firm.

1. Pricing–at and/or over Italian Swiss Colony and Gallo.
2. Packaging.
3. Advertising. [76]

C. Use Franzia production as source of supply for other table wine entries:

1. Tribuno.
2. Jug. (CX 681C)

247. In October of 1973, the president of Coke-New York, in a letter to the president of Franzia, discussed plans to hold "some preliminary coordination meetings regarding possible joint production and marketing efforts" by Mogen David and Franzia and foresaw "more formal planning meetings involving the management of both Mogen David and Franzia near the end of the year to work on very specific marketing and production plans for 1974" (CX 778A-B).

248. By November 20, 1973, Mogen David officials were considering establishing "dba's" for some Mogen David and Tribuno products out of Ripon, California (CX 566).

249. On December 6, 1973, Joseph S. Franzia, Franzia's national sales manager, met with Edward S. Nemo, Mogen David's national sales manager, and discussed the possible consolidation and development of the "Franzia label and the Mogen David label market by market" for the 35 non-control states and the District of Columbia (CX's 781A-E, 681B). The production potential of Franzia for Mogen David products was also discussed (CX 781A).

(2) Post-Acquisition Consolidation

250. After the acquisition of Franzia, Mogen David officials were made responsible for the selection of new Franzia distributors and its sales and shipments of wine, as well as other matters, such as the hiring of Franzia's regional managers who reported to officials of Mogen David (CX's 562, 569, 678A-C). Franzia's national sales manager reported directly to Mogen David's director of sales, and Mogen David was furnished with market planning forms completed by Franzia salesmen (CX's 654A-B, 659A-C, 854B). [77]

251. Mogen David and Coke-New York officials participated in planning pricing strategy for Franzia's wines, and Franzia arranged to have Mogen David personnel provide it with competitive pricing information (CX's 219, 653A, 838).

252. After the acquisition, Mogen David became the sales agent for Franzia wines in 14 control states (CX 60C). By June 1, 1974, Franzia and Mogen David agreed that Mogen David's sales force would be the sales agents for all Franzia products (CX 574B), and Mogen David took over "the selling and dealing with the wholesalers

for the Franzia Brothers for all the Franzia wines." (CX 833; Tr. 707-08). Mogen David salesmen promoted Franzia wines to wholesalers and, in some instances, retailers (CX's 194, 216, 226, 235, 280A, C, 407A, 410B, 511A), and helped to place Franzia in restaurant accounts (CX's 536, 537, 538).

253. In some instances, Mogen David salesmen transferred the Franzia line from its distributors to Mogen David distributors (CX's 175A-B, 269A, 393A, 400A-B). The Franzia sales force began to distribute Mogen David wines on July 1, 1974, and the letter announcing this predicted that it would give Franzia new accounts (CX 571A). Franzia acted as sales agent for Mogen David 20 20 in February 1975 in California, opened new accounts for 20 20 and seems to have improved 20 20 sales (CX's 567, 880A, E, P-Q).

(3) Changes in Franzia's Advertising and Pricing Policies

254. Prior to its acquisition by Coke-New York, Franzia had a reputation as a company that competed largely on the basis of price (Tr. 225, 359, 565), and its advertising and promotional expenses for the five fiscal years prior to the acquisition were not substantial:

Years Ended	
April 30, 1969	$ 55,000
April 30, 1970	60,000
April 30, 1971	43,000
July 31, 1972	143,000
July 31, 1973	232,000

(CX 97)

[78] 255. Franzia media advertising increased for a few years after the acquisition. In calendar 1973, it was $298,691; for 1974 it was $174,279; and by 1975, it increased to $789,432. In 1976, advertising declined to $200,831 (CX 716Z15).

256. After the acquisition, Coke-New York repositioned the Franzia line of wines (CX's 532A-F, 549A-D, 682A-F; Tr. 790-800, 1201). This included new packaging, new wine blends, premium dessert wines and premium varietals (CX 682A-B). Coke-New York boasted that "Franzia's 'New Shape' campaign will be supported by the company's most expensive and far-reaching advertising program in its history. Spot television ads will run in 20 markets across the country at a rate translatable to $5 million on a national basis" (CX 682A).

257. Coke-New York hired a package design agency to redesign

Franzia's packaging; it also hired an advertising agency, Grey Advertising (Tr. 788–89). In March 1974, a consumer marketing department was established at Franzia for the purpose of developing new packaging, advertising, point-of-sale materials and new products (CX 574B-C).

258. The director of marketing for Mogen David recommended that an analysis be conducted to determine whether Franzia wines could be sold at higher FOB, retail list and shelf prices (CX 576A), and in July 1974, Mr. Arthur Ciocca recommended that Franzia raise its prices (CX 535A-B). Franzia's prices were in fact raised subsequent to the acquisition–"well over 10%" (CX 550G; Tr. 883–87, 1201).

(4) Franzia's Role in the Production of Mogen David Wines

259. Coke-New York planned to have Franzia produce wines for Mogen David in California. This proved to be impossible (Finding 227); however, Franzia did produce grape concentrate for Mogen David and vermouth for Tribuno as well as some pop wines that were apple and strawberry based (Tr. 778, 1811–12; CX's 565A-B, 782M), and Mogen David currently obtains blending wines, concentrates and high proof from Franzia (Tr. 1150). **[79]**

260. At one time, Franzia produced a table wine for Mogen David under the "Fanfaron" label (CX 882A), but the wine was not a success and it was discontinued (Finding 64).

261. Franzia now produces standard California red and white wine concentrate, Chenin Blanc and French Colombard wine for use in production of the new Mogen David Light wines (CX 1041B-C). California grape juice or concentrate is also used in substantial quantities in the production of Mogen David wines (CX 716Z19).

(5) Distributor Realignment

262. The term "leverage" as used in the wine industry is the threat–actual or implied–that a large supplier with a fast moving brand is able to use to force a distributor to carry the slower moving brand or lose the entire line (Tr. 434, 440–41, 449, 1507–08, 1566. See also Tr. 713, 1319, 1364).

263. Mogen David officials believed that it had "considerable volume potential and distribution leverage because of the volume of all Mogen David products" (CX 24Z4), and on other occasions, consultants or Coke-New York officials recognized the potentiality of leverage (CX's 17V, 18Z37, 559B, 680C, E-F).

264. After the acquisition, sometime in January or February

1974, Coke-New York held a meeting of Franzia's and Mogen David's regional sales officials. Mr. John Borders, at that time Franzia's coordinator for national sales, testified that:

> The purpose of the meeting was to go over all of the wholesalers, both Mogen David, Tribuno and Franzia by market to see where we could consolidate whenever possible into one wholesale distributorship (Tr. 698).

Every Franzia and Mogen David distributor was discussed, and the tendency was to suggest moving the Franzia line into the Mogen David distributor, rather than the other way around (Tr. 703). [80]

265. As of October 17, 1977, of those distributors who were then currently distributing both Mogen David and Franzia products, at least 16 were Mogen David distributors who began to distribute Franzia after the acquisition (CX's 716, 980G-H). Distributors who were added as of June 7, 1974 were located in Wisconsin, Illinois and Ohio, and totaled 27 (CX 60E). Other states were North Carolina (CX 716Z12), Virginia (CX 716Z14), South Dakota (CX 716Z13) and Missouri (CX 980G).

266. There are additional Mogen David distributors that had also taken on the Franzia line subsequent to the acquisition, but may not currently be carrying both lines. For example, in Ohio, Franzia was placed in 19 additional Mogen David houses (Tr. 856–57).

267. In some cases where Franzia was placed in a Mogen David house, its distributors were terminated. National Brands was terminated as the Franzia distributor in Miami in May or June of 1974 although, in Mr. Borders' opinion, it was an effective distributor for Franzia products (Tr. 712).

268. By June 7, 1974, Coke-New York had terminated a total of seven Franzia distributors located in Alabama, South Dakota, and Milwaukee, Hurley, Madison and Appleton, Wisconsin (CX's 60E, 74A-B, 173, 175A; see also CX's 557, 670, 671, 805; Tr. 706–07).

H. Effects of the Acquisition

(1) Consolidation of Lines

269. After Coke-New York acquired Franzia, Continental Distributing Company, which sold Mogen David, took the Franzia line (Tr. 85). Continental also distributed CWA wines (Tr. 81). After the acquisition, according to Mr. Perelli-Minetti of CWA, its sales to Continental declined so much that it had to find another Chicago distributor in May of 1977. Mr. Perelli-Minetti attributed this decline to "the pressure that had to come from. . .the Mogen David, Franzia, and Tribuno relationship" (Tr. 84–85).

270. Mr. Perelli-Minetti's conjecture is not supported by the record. Continental had contacted Franzia before the acquisition about distributing its [81] wines (Tr. 659) and it is likely that the decision to distribute Franzia was a result of its interest, not because of the acquisition. CWA's declining sales to Continental, rather than a result of pressure from Coke-New York, could just as likely have been because Continental was paying less for Franzia's wines (Tr. 146, 468). Mr. Perelli-Minetti's other claims regarding the effects of the acquisition on CWA's business in other areas of the country are so vague that they do not warrant consideration (Tr. 86–87).

271. Mr. John Simon, of Bardenheier's Wine Cellars, testified that Jule Fisher, a distributor in Belleville, Illinois, had been distributing his company's and Mogen David's wines for several years before the acquisition. In 1974 or 1975, Fisher dropped Bardenheier and took on Franzia's wines. Although Bardenheier obtained a new distributor, its sales have declined (Tr. 1559–60). However, Bardenheier still sells its wines to a distributor in Columbia, Missouri, which also carries Mogen David and Franzia wines (Tr. 1560–61).

272. Mr. Ernest Haas of East-Side Winery testified that the consolidation of Mogen David, Franzia and Tribuno into a single distributorship would affect his company's sales because the distributor would place greater emphasis on Coke-New York's wines than on weaker brands (Tr. 226–27), yet he stated on cross-examination that "so far" the acquisition has not hurt his business in any way and that it was fairly low down on his list of competitive concerns (Tr. 254).

273. Mr. Fred De Pompei, A Cleveland distributor, testified that if he carried the full Mogen David line he would certainly accept Franzia out of fear of losing the Mogen David line (Tr. 1311–12).

274. Consolidation of Mogen David and Franzia in the same distributors can be predicted, say complaint counsel, on the basis of Coke-New York's actions when Tribuno was acquired.

275. Prior to its acquisition, Coke-New York planned to sell Tribuno products through the Mogen David sales force (CX's 7G, 33L, 35). In a memo [82] submitted to the president of Mogen David after the acquisition, the Mogen David product manager (identified in CX 721B) stated:

> Some proposed changes for strengthening market conditions by consolidating the Tribuno brand with Mogen David distributors have been implemented. Additional moves to solidify other marketing areas will be considered as management evaluates further data. (CX 48B).

Subsequent to the acquisition of distribution rights from Twenty-One Brands, Coke-New York, terminated some wholesalers of Tribuno products and moved the Tribuno brand to wholesalers of Mogen David products (Tr. 1123–27). At present, of 286 Mogen David distributors, 195 (68 percent also carry Tribuno products (CX's 716z8-14, 980G-H)).

276. Nevertheless, I do not believe that Mogen David and Franzia will be consolidated in a substantial number of distributors against their will, or that Mogen David distributors will "volunteer" to take on Franzia because of fears of losing the Mogen David line.

277. First, consolidating these lines might not be best for Mogen David or for Franzia. For example, Mr. Marvin Sands of Canandaigua said that "[a] good distributor for [its] wines would actually vary with what specific wine. . .or what specific brand of wine" Canandaigua was selling in the market (Tr. 1359). In fact, of Canandaigua's 300 distributors for its popular Wild Irish Rose, only 20 to 30 carry its Bisceglia brand of California wine (Tr. 1405–06).

278. A second restraint upon consolidation of product lines is the increased protection given to the distributor by state franchise laws and the development of protective case law. Where they exist, they have weakened whatever leverage suppliers may in the past have been able to exercise (Tr. 107–08; 243). Arizona, Connecticut, Georgia, Massachusetts, Nevada, New Jersey, New Mexico, Ohio, Vermont, and Wisconsin all have statutes that, in general, forbid termination of distributors except upon a showing of good faith and good cause [83] (Ariz. Rev. Stat. §§ 44–1566 to 1567; Conn. Gen. Stat. Ann. § 30–17; Ga. Dept. Rev. Regs. § 560–8–7–.08; Mass. Ann. Laws Ch. 138 § 25E; Nev. Rev. Stat. §§ 598.290–.350; N.J. Stat. Ann. §§ 33:1–93.6 to .11; N.M. Stat. Ann. §§ 46–9–16 to 20; Ohio Rev. Code Ann. §§ 133.82–.87; Vt. Stat. Ann. Tit. 7 §§ 701–708; Wisc. Stat. Ann. §§ 135.01–.07); Kansas and Oklahoma require suppliers to sell to all distributors; in addition, Oklahoma forbids conditioning sales of one brand on acceptance of another brand (Kan. Stat. § 41–1101; Okla. Alc. Bev. Cont. Bd. Regs. Art. 3 § 1).

279. In the words of one distributor, "a supplier cannot just move his lines just because he thinks it would be nice to move them down the street" (Tr. 2007–08). Lawsuits by terminated distributors are increasingly common, are advertised on the distributor grapevine, and can be very costly to suppliers (Tr. 244–45). Personal experience led East-Side Winery's Mr. Ernest Haas to conclude that, at least in Wisconsin, "any distributor is more powerful than the supplier" (Tr. 227, 243, 257). Outside Wisconsin, he has found the situation to be the same (Haas 244–45).

280. Robert Setrakian of California Growers Winery described the reality of attempting to leverage one product into a distributor on the strength of another this way:

> I think it would depend on whether that distributor, one, needs a line of products comparable to the [offered] line, and if he does need it, and the [new]. . .line. If he didn't have it and didn't need it, I don't think anybody could make him take it on. (Tr. 372).

281. Complaint counsel's theory is refuted by specific examples of producers' failure to consolidate lines and the independence of distributors.

282. In February 1976, a 19 percent ownership position in Sonoma Vineyards was acquired by Renfield Corporation, a large importer of such well-known brands as Gordon's gin and vodka, Remy-Margin cognac, and Martini & Rossi vermouth (CX 1009V). Sonoma needed management help from an established [84] company because previous management decisions (notably, over-expansion) had put the company "under a critical financial strain." (Tr. 1740–42, 1745, 1772). Despite common ownership, however, Sonoma's small sales force does not include any former Renfield personnel. Choosing to ignore the 100-man Renfield sales force as unsuitable, Sonoma insisted that Renfield set up a separate sales division of eight people to sell only Sonoma wines. All eight Sonoma salesmen were experienced in wine sales and specially hired by Renfield under Sonoma's direction (Tr. 1760–61).

283. Renfield has a national network of about 250 distributors (Tr. 1759). However, of these 250, Sonoma has appointed only 70 to 80 to distribute its wines (Tr. 1748). Sonoma has at present about the same number of non-Renfield distributors and expects in future to add more, mainly non-Renfield, distributors (Tr. 1760–61).

284. Neither of Sonoma's distributors in Denver, for example, is a Renfield house; one is a new distributor and one is a beer distributor (Tr. 1994–95). John Anderson, the president of Sonoma, described the process as "market-by-market" appointment of whatever distributor the individual competitive situation calls for (Tr. 1748, 1769). The commercial necessity of Anderson's approach, instead of a policy of consolidation, is underscored by Renfield's previous experience with a line of imported Italian table wines marketed under the well-known Buitoni label. Those wines, sold by the Renfield sales force through the Renfield distribution network, were "a conspicuous failure in the marketplace." (Tr. 1762).

285. Hiram Walker-Gooderham & Worts Limited, distiller and importer of such major brands as Canadian Club whiskey; Ballan-

tine's scotch, Booth's gin, Courvoisier cognac, Kahlua liqueur, Frederick Wildman wines, and Jules Berman wines, uses three entirely separate distribution networks for its wine products. Comparison of distributor lists for the three Hiram Walker subsidiaries-Frederick Wildman & Sons Ltd., Jules Berman & Associates, Inc., and W.A. Taylor & Company-shows almost no common distributors (RX's 212A-F, 213A-E, 214A-J; Tr. 2331). [85]

286. Taylor Wine Company, which ranked sixth in total wine sales in 1973 (CX 991A), has two major product lines, Taylor and Great Western, distributed by two entirely separate distributor networks. Comparison of distributor lists for the two divisions shows almost no overlap (RX's 356A-Z48, 357A-Z43).

287. The two Almaden distributors with which Michael Gelven deals in Massachusetts do not carry any of the products of Almaden's $1.5 billion distillery parent, National Distillers and Chemical Corporation (RX 27C; Tr. 2216-17). MP Beverages in Lawrence, Massachusetts carries Narragansett beer and Roma and Almaden wines. Another distributor in the market carries the National Distillers liquor products (Tr. 2216-17).

288. Gibson Wine Company, which makes both conventional wines and fruit and berry wines (including Concord), often distributes those two product lines through different distributors (Tr. 514, 520) and Franzia had distributors who carried table wines but not the sparkling wines (Tr. 714).

289. Mr. John Pearson of C & C Distributing, 75 percent of whose wine sales are of Franzia products, flatly refused to take on the Mogen David product Fanfaron in the quantities Mogen David wanted because he did not think it would sell in the quantities Mogen David projected[34] (Tr. 2006-08).

290. Mr. Gary Raden, 60 percent to 75 percent of whose entire business is Franzia wine, and who credits the growth of his business to his Franzia products, carries only 15 percent to 20 percent of the Franzia product line (Tr. 1823-24). He has applied to be, and is being considered for appointment as, a Mogen David distributor, but he would not like to sell Tribuno vermouth because it is too high priced (Tr. 1825, 1847-48, 1853).

291. Mr. Perelli-Minetti of CWA testified that in some instances the best choice is exactly the opposite of consolidation: to split lines among distributors [86] in order to create competition (Tr. 127-28). From the distributor's point of view, a broad line resulting from

[34] Fanfaron was also not sold in the Mogen David house in Houston (Tr. 1220-21).

consolidation is not necessarily best, since profit margins are more important than sheer volume (Tr. 690–91).

292. Consolidation of the Mogen David and Franzia lines might also be hampered because of the fact that nearly three out of four Mogen David distributors are distributors of Gallo or United Vintners wines. Because of their sales leadership (RX 418A), the presence of these companies may foreclose smaller competing brands including Franzia from those distributors.

293. Mr. J. S. Franzia stated that a distributor "can't do justice to two masters" when one of them is Gallo or United Vintners and the other is Franzia; Gallo and Franzia as masters are "like General Motors and Hudson" (Tr. 671). Mr. Perelli-Minetti stated that he would not put California Wine Association's products—directly competitive with those of Franzia—into a Gallo house. "Not if I can help it, because we get murdered if we are in there" (Tr. 64, 114).

294. Meyer Robinson, general manager of Mogen David's chief competitor Manischewitz, asked to decide whether, if president of Franzia, he would put Franzia in a Gallo wholesaler said that he would not (Tr. 1466–67). On redirect he stated:

> MR. BROWNMAN: You indicated that you probably would not put Franzia in a Gallo house. My question is, if it were that or no distribution at all, would you put Franzia in a Gallo house?
>
> MR. ROBINSON: I couldn't see it.
>
> MR. BROWNMAN: Would you rather have no distribution or some distribution?
>
> MR. ROBINSON: I probably wouldn't have any distribution if I went into a Gallo house. (Tr. 1477).

[87] 295. Mr. Robinson went on to say that "it would be better off for them not to go into that market" rather than go into a Gallo house, even with a separate sales force (Tr. 1478). Mr. John Anderson, president of Sonoma Vineyards, also believes Franzia should not be placed in Gallo or United Vintners houses (Tr. 1769).

296. Since the competitive forces facing Manischewitz are wholly different from those facing Franzia, Mr. Robinson has no qualms about putting the Manischewitz products in a Gallo house. However, he shares a distributor with Mogen David only reluctantly and only in three instances in the United States out of a total of more than 200 Manischewitz distributors (Tr. 1452).

297. Actual events reveal that future consolidation of Mogen David and Franzia distributors is not probable. As discussed above, soon after the acquisition, Mogen David salesmen began to sell Franzia and some Mogen David distributors were given the Franzia line, a few by transfers from existing distributors and more by new appointment in previously unserviced areas (Tr. 834–35, 856).

298. The broadest single attempt to gain new distribution for Franzia by the use of Mogen David distributors occurred in Ohio during the nine months when Mogen David was responsible for sales of Franzia (CX 701B; Tr. 857). Mogen David placed Franzia in 18 or 19 of its distributors in Ohio, most of which were Gallo houses (Tr. 857). However, after initial inventory sales to the distributors, Franzia sold virtually nothing more and before it withdrew was ultimately forced to buy back much of the inventory, which had spoiled (CX's 701B, 862B; Tr. 860).

299. In New York City, the Mogen David sales force pushed Franzia out of its leading distributor in the United States, Robinson-Lloyds Ltd., and into the local Mogen David house (CX 613; Tr. 1786–87). That distributor proved totally ineffective for Franzia and New York sales fell from approximately 250,000 cases per year to almost nothing (Tr. 959–61). Franzia has since reconciled its differences with Robinson-Lloyds and today is again doing business with that company, although sales have not yet returned to their previous level (Tr. 959–61, 1793–94). [88]

300. After August 1974, because of a dispute between Mogen David's and Franzia's management over Mogen David's inability to sell Franzia wine (Tr. 717), Coke-New York decided to separate their sales organizations (CX's 554A–B, 555A–H, 560, 561A–F; RX's 103, 404A–P; Tr. 852–69, 1196–98). As of January 1, 1975, total separation was in effect, has continued to date, and according to Coke-New York's executive vice president, will be maintained in the future (Tr. 1198).

301. After reviewing the above evidence, I find that the acquisition of Franzia will probably not have any substantial adverse effect on the ability of other producers to distribute their wine, and that it will not foreclose a significant number of distributors and sales representatives of Franzia products from a "high volume, fast moving account" (Cplt., Par. 21d).

(2) Entry

302. Complaint counsel say that the wine industry is "highly capital intensive" (CX 27L, Z34; Tr. 353, 378–79, 1756, 2065, 2180, 2307), that small producers cannot spend the money which they need to grow (Tr. 378–79, 351–52, 2064), and that, with one exception such new entry as there has been since the 1960's has been at the premium level (CPF 180).

303. However, that exception—Bronco—discloses that even in this concentrated industry, it is possible for a significant new entrant to appear.

304. The day after Coke-New York completed its acquisition of Franzia, three Franzias resigned from the winery (Tr. 1184, 1192). These members of the younger generation of the Franzia family had been, respectively, vice president and director of national sales, vice president-sales, and vice president-operations (CX 723). They were the core of Franzia's management before the acquisition and are regarded as knowledgeable, competent, and aggressive about the wine business (Tr. 254, 1785).

305. The day they left Franzia, the young Franzias started a new winery. Their aim was an efficient, family-held winery that would be aggressively competitive in the [89] sale of conventional California jug wines (Tr. 606, 609). The product was to be "a high quality wine for the consumer at the lowest price possible." (Tr. 614).

306. Using less than $1 million in equity, they borrowed approximately $3 million from the Bank of America and began in June 1974 to build a winery in Ceres, California. Construction was rapid and the first bottling took place on September 30 of the same year (RX 50; Tr. 608–10, 621–28). Capacity of the new winery was one million gallons, which has since grown to 1.75 million (Tr. 612). Bronco is also the operating partner in a joint venture (with Getty Oil Company) that owns a four-million-gallon winery in Fresno, California. That winery has just recently been constructed (Tr. 620–21).

307. Taking advantage of one of the industry's periodic oversupply conditions, Bronco eased the path of entry by buying bulk wine through brokers and finishing it in its own winery (Tr. 613–14). Bronco described itself as [see *In Camera* Findings] (RX 52A). During 1974, bulk red wine sold for prices between 25 cents and the low 30's per gallon, prices at which neither Bronco nor its competitors could have made the wine (Tr. 615–16, 898–99). Bronco's sales increased to 1,350,000 cases in its first year—approximately one-third the size of 40-year-old Franzia—and the company quickly integrated its facilities (Tr. 635, 679).

308. Bronco's key to success in the marketplace was price: "[t]hey did it on price. . .there is no one selling wine as cheap as they have been in recent years. . . ." (Tr. 1583). Bronco's November 1977 prices were 99 cents per quart and $1.99 per gallon of its JFJ wines and $1.99 per fifth of champagne, price levels for branded products that are competitive with private label prices in California (Tr. 666–67). Bronco's sales have been growing steadily (Tr. 679).

309. Although sales of branded products within California account for almost all of Bronco's volume, the company has been able to obtain distribution (and subsequent sales) in numerous other states, and [see *In Camera* Findings], including: Arizona, Florida,

Oregon, Missouri, Nevada, New Jersey, New York, Texas, [90] Washington, [see *In Camera* Findings] (RX's 50E–G, 51E, 52E; Tr. 637–38). Distribution and sales outside California have been obtained despite Bronco's having made no active effort to seek them (RX 52D; Tr. 639–41, 672, 688–89). Within California, Bronco is its own wholesaler and has obtained distribution in five major supermarket chains in the northern part of the state. The company has done no advertising and plans to do none (Tr. 668–69). Although Bronco made no profits in 1974, 1975 or 1976, its owners were confident about 1977 profits (Tr. 641) and the future of the company (Tr. 673).

310. California Growers Winery, founded in 1936, was a farmers cooperative selling bulk dessert wines and bulk brandy; it did not produce any bottled wine products (Tr. 330). By 1971, the cooperative was virtually dormant and was reorganized as a corporation under new leadership (Tr. 333). Robert Setrakian, who had not previously been in the wine business (although his family was), assumed control of the company and California Growers entered the branded wine business for the first time (Tr. 330–31). Mr. Setrakian testified that California Growers was "sort of" a new entrant and that, as far as he was concerned, "March 1971 was the day that [he] was weaned into the wine industry" (Tr. 379–80).

311. Beginning in 1970 with a crush[35] of 4,000 tons of grapes and no branded sales, California Growers has grown impressively (Tr. 334, 381). The winery, with 15 million gallons of storage capacity, crushed 95,000 tons of grapes last year, which would produce 16 million gallons of wine if used entirely for dry wine (Tr. 342, 396). Sales of case goods, under the company's own brands and private labels, were between 800,000 and 1 million cases, or between 2.5 and 3 million gallons (Tr. 362, 381).

312. Although it does not advertise because it does not have the necessary capital, California Growers has gained distribution and sales for its branded [91] products in approximately 27 states, including California, Florida, Illinois, New Jersey, New York, Ohio, Texas, and in Puerto Rico (RX 57A–B; Tr. 339, 383). Sales are strongest in northern California, because much of the company's manpower is located there, Californians drink 25 percent of the wine produced in the state, and—despite the lack of advertising—one of the company's brands simply "caught on" there (Tr. 340).

[35] All the grapes crushed for winemaking in a single harvest season (Tr. 273).

313. Although Mr. Setrakian did not paint a completely rosy picture of his experiences in the wine industry,[36] he was generally optimistic about his company's future:

> I'm optimistic about the industry. We are not in the buggy whip industry, and I'm optimistic we have the wherewithal of maintaining ourselves and increasing our case goods sales at some time. We are going to get rid of all these guys[37] that should be doing what they were doing before they got in the wine business. (Tr. 400).

Regarding the possibility of the entry of other companies into the wine business, he said:

> A chimpanzee could have come into this business in 1971. It was a very romantic, highly—it had a high exposure, it was highly touted, both by the investment banking community as well as commercial banks, and if one had reasonable credentials, one could get into this industry with comparative ease. (Tr. 381). [92]

314. About 1953, Sebastiani Vineyards, which had been a supplier of bulk wine for many years, gradually began to enter the bottled wine business (Tr. 2284). Once it entered the branded business, Sebastiani's sales grew slowly until 1970 or 1971 when the last bulk wine was sold (Tr. 2285–86). At that point, sales through the company's 40 or 50 distributors were 90 percent in California (Tr. 2309–10). Slow growth ended when Sebastiani's sales "exploded" in 1971 (Tr. 2285). Sales in 1975 were double those of 1974; sales in 1976 were 38 percent greater than in 1975; sales in 1977 were 53 percent greater than in 1976 (Tr. 2286). Thus Sebastiani's sales have increased from 709,000 gallons in 1970 to approximately 5,222,000 gallons in 1977; *i.e.,* 1977 sales are more than 636 percent of what they were seven years ago (RX 350; Tr. 2286).

315. Mr. Sebastiani believes that his company's growth rate is the fastest in the industry. Its growth cannot be attributed to enormous advertising expenditures,[38] but to "a lot of hard work. . . . An honest product at a reasonable price. . .and sheer luck" (the "terrific explosion" in the interest in wine) (Tr. 2289–90, 2312–13).

316. Mirassou Vineyards started, like Sebastiani, as a producer of premium bulk wine (Tr. 2028–29). The Mirassou family has been making wine in California since 1854; until 1966, however, fewer than 1,000 cases per year of its output were put in bottles (Tr. 2029–30, 2405).

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[36] We are going through what I hope the result is going to be. we are going through a growth process right now, and it's costing us a hell of a lot of money, and the competition is fierce, and the cost of production is monumental, and labor is going insane, as is the cost of energy and the cost of glass and the cost of corks, and if I ever had it to do all over again, I would probably do it anyway. (Tr. 379).

[37] Such as Pillsbury and Nestle (Tr. 353–57).

[38] Although Mr. Sebastiani spent $450–500,000 in 1977 for media advertising (Tr. 2306), it spent less than this during the early years of its growth.

317. Responding to the needs of a new generation in the Mirassou family for an expanded business, the winery began to sell wine under the Mirassou label for the first time in 1966 (Tr. 2030). Despite starting with no consumer franchise, no sales or marketing force, and no experience in the bottled goods business[39]—and [93] without any media advertising—Mirassou has grown from sales of 1,000 cases in 1966 to 165,000 cases in 1976 and 285,000 cases in 1977 (Tr. 2033, 2056).

318. This growth has been achieved by the five youngest family members themselves, who after finishing college decided that it was "time to put the Mirassou label on the market and let it be known." (Tr. 2030). The youngest generation began "pounding the pavement and beating on doors of retailers and wholesalers and getting people acquainted with [the] wine little by little. . . ." (Tr. 2030-31). The result has been, despite the lack of any training on the part of its marketing manager (Tr. 2034) and the refusal to advertise (even though the company can afford it) (Tr. 2033), that Mirassou's wines are now distributed nationally by about 150 distributors (Tr. 2031).

319. Perhaps more representative of the bulk of new entrants than the companies discussed above is Mt. Veeder Winery, which was started in 1971 by Mr. Michael Bernstein, a former FTC attorney (Tr. 1871-72). Starting with a capital investment of $126,000 for the winery and $25,000 for the original land (Tr. 1874-77, 1928-29), Mt. Veeder's sales grew to roughly 1,000 cases in 1976 and 1,450 cases in 1977, plus 900 cases of a lower priced second label (Tr. 1888-89).

320. Mt. Veeder's wines are very expensive (Tr. 1938, 1953) and its production, even at capacity (2,700 to 2,900 cases) (Tr. 1888-89) is so small that it can have no possible effect on the structure of the industry; however, its story shows that even one who is totally inexperienced can enter this industry (at a very modest level, it is true) with little capital outlay. The reason is that wine producers are cooperative with and actually encourage new entrants (Tr. 1879, 1919-20, 1957). Other reasons include the growth of interest in wine (Tr. 1910-11) and the free advertising by newspapers and magazines which seek out and publicize new wines and wineries (Tr. 1892-1901, 2212, 2293-94).

321. Although Mr. Bernstein has chosen to keep Mt. Veeder Winery small, he believes that expansion would be very easy (Tr. 1889, 1903). In its present [94] hillside location, where in his judgment vineyards produce the finest grapes, Mt. Veeder could

[39] At the time it went into the case (bottled) goods business, Mirassou's winery had an 800,000 gallon capacity and sold bulk wine to companies like Almaden, Paul Masson, Gallo, and Bear Mountain (Tr. 2052).

double its capacity (Tr. 1903, 1932). Growing tenfold would require building a facility in the Napa Valley, which he believes could readily be done (Tr. 1904).

322. Mr. Bernstein regards Inglenook as a model for even greater expansion: a very fine reputation for high quality, which Mt. Veeder has already achieved, can be used to increase demand for lower cost wines from different grape varieties (Tr. 1905–06, 1943–47). Mr. Bernstein is confident that he could finance such expansion himself and that Mt. Veeder's present distribution could be extended without any significant difficulty (Tr. 1906–07).

323. Canandaigua Wine Company's 1974 acquisition, Bisceglia Brothers, can be viewed as a new entrant in the popularly priced segment of the conventional wine business. Bisceglia had sold bulk wine before 1974, had no consumer franchise or brand recognition, and was almost insolvent (Tr. 1398). Nevertheless, Canandiagua is optimistic that Bisceglia can achieve a meaningful level of sales and be profitable (Tr. 1402–03).

324. Canandaigua, a major eastern producer of specialty products, was itself started with only a $20,000 investment about 30 years ago (Tr. 1400). Bisceglia, which Canandaigua describes as a complete major wine producing facility with 4.5 million gallons in capacity, cost Canandaigua only $1.5 million (RX 59H, N).

325. Aside from the specific examples discussed above, the total number of new entrants actually producing wine in commercial quantities in the past 11 years is hotly disputed by the parties. Coke-New York contends that yearly summary statistics published by the Treasury Department shows a "stunning growth" in the number of wineries engaged "in the business. . .of producing wine" (RPF 203). Complaint counsel counter that even if the figures are correct, they are merely numbers and do not show whether the listed wineries are in actual commercial production or, if they are, the extent of their production (CRF, p. 64). [95]

326. This is true; on the other hand, each of the wineries is producing more than 200 gallons of wine per year, since production of that amount or less for non-commercial use is completely exempt from tax and bonding requirements (26 U.S.C. 5042; 27 C.F.R. 240.540). Furthermore, each winery must hold a federal permit issued by the Bureau of Alcohol, Tobacco and Firearms of the Department of the Treasury (27 C.F.R. 1.21). Such permits are issued to a wine producer upon presentation of a surety or collateral bond of at least $1,000 and only if "by reason of his business experience, financial standing or trade connections [he] is likely to commence operations as a . . . wine producer . . . within a reasonable period

and to maintain such operations in conformity with Federal law," (27 C.F.R. 1.24, 240.120, 240.221), and a failure to engage in the commercial operations authorized by the permit for more than two years will result in proceedings to revoke it.

327. Finally, although admitted with the limitation that there be no reference to the information about specific wineries listed in it, a 1977 directory published by Wines & Vines is in relatively close agreement with the federal statistics, counting 575 commercial wineries in the United States as of December 31, 1976, nearly matching the federal figure of 585 as of September 30, 1976 (CX 986; Tr. 1393–94).

328. Thus, while the following chart does not reveal their commercial significance, it does show that there have been several new entrants into the wine industry over the past 11 years.

Fiscal Year	*Wineries*	*Increase Over Previous Year*
1977	652	67
1976	585	39
1975	546	34
1974	512	32
1973	480	32
1972	448	10
1971	438	3
1970	435	3
1969	432	4
1968	428	4
1967	424	2

(RX's 368H–I; 369F–G, 370C–D, 371F–G, 372G, 373I, 374I, 375J, 376I, 459K, 460B). **[96]**

329. There is, in my opinion, a potential for significant growth by these new entrants, for from 1967 to 1976, adult per capita consumption of wine in the United States increased from 1.738 gallons per year to 2.750 gallons (RX 380L), and it will probably increase still further in the future although perhaps not to the extent that the United States will be a wine-drinking country in the sense that European countries are (RX 52A; Tr. 231, 282–83, 470, 567, 1910–11, 2040, 2296–97). Coupled with population increases, the increase in per capita consumption has brought about an enormous growth in the amount of wine produced: the total has nearly doubled in 10 years, soaring from 203.4 million gallons in 1967 to 400.3 million gallons in 1977 (RX's 378J, 501).

330. Complaint counsel recognize the substantial increase in

wine consumption in the past 10 years but point out that it was accompanied by a substantial increase in concentration (CRF, p. 64). This is not completely true, for as of this date it cannot be said that there is any trend toward concentration in the industry (Finding 245) even though sales are continuing to climb.

331. Complaint counsel also seem to suggest that the entry of Bronco, California Growers, Sebastiani, and Mirassou as significant producers of wine prove little because their principals had prior experience in the industry. I cannot accept this argument, for they brought to the new companies (or the new products) no overwhelming advantages which they obtained from that experience. They did not rely extensively on advertising or existing distributor networks, yet they were able to enter and expand their production.

332. On the basis of the above evidence, I must conclude that barriers to entry in the wine industry are low, that they can be overcome by companies run by experienced personnel with relatively modest financial backing and that, with prudent management, these companies can become significant producers of wine. Nor have complaint counsel established that Franzia's acquisition by Coke-New York will increase these modest barriers to entry. [97]

(3) Concentration

333. Although four and eight firm concentration in the wine industry increased substantially from 1968 to 1971 (Findings 243–44), the picture from 1971 to 1976 was quite different; during this period of time, four firm concentration was only 0.67 percent higher than 1970 (Finding 245). These figures reveal that at present there is no trend toward a significant increase (or decrease) in four firm concentration in the wine industry.

(4) Trend Toward Mergers and Acquisitions

334. Complaint counsel have not proved that there is a trend toward mergers or acquisitions in the wine industry, or that the Franzia acquisition will encourage future mergers or acquisitions.[40]

(5) Elimination of Franzia As an Aggressive Competitor

335. While Coke-New York contemplated changing Franzia's competitive posture from one of high volume-low price, the attempt failed and caused a sharp drop in sales until Franzia brought its prices in line with competition (Tr. 886–92, 1200–02). Today, Franzia

[40] Complaint counsel's only reference to acquisition history in the wine industry is the challenged acquisition, Renfield's connection with Sonoma, and Canandaigua's acquisition of Bisceglia (Brief, p. 19).

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is an aggressive price competitor (Tr. 145–46, 306, 390, 467–68, 1513, 1820–21).[41]

336. Initially, Mr. Ciocca, Franzia's new marketing manager (now its president) believed that it could raise prices (Tr. 799), and under pressure from Coke-New York to increase revenues through price increases, [98] Franzia in three months in 1974 raised its California prices on gallons from $2.99 to $3.49 (Tr. 887, 1201). Sales on this single item, in a state accounting for 60 percent of Franzia's sales, fell by half, from a rate of 300,000 cases down to 150,000 cases. Despite the price increase, the net effect on revenues was negative because of the drastic decline in volume (Tr. 886–88).

337. In 1975, again in California, Franzia began a programmed series of price increases on fifths (Tr. 889–90). According to Mr. Ciocca, Franzia's president, movement of its wine through the stores "stopped" as consumers refused to accept the higher prices (Tr. 890). The chain stores reacted by saying "you have raised yourself out of business." (Tr. 891). Franzia retreated and in the autumn of 1975 cut prices back to their original level, which to some extent restored its sales (Tr. 892).

338. There is little likelihood that Franzia will repeat this attempt or that if it did, it would be any more successful than in the past, for it will always be faced with vigorous competition in popular priced wines (Findings 67–77). Unlike Coke-New York, which has a consumer franchise (Tr. 1784), and which can probably ignore lower-priced competition, Franzia must always be aware of, and meet, its competitors in terms of quality and price (see Tr. 1790); therefore, I find that the acquisition will not significantly alter Franzia's pricing policy, and that Franzia will remain as a substantial, independent factor in the wine industry.

(6) Elimination of Actual and Potential Competition Between Franzia and Coke-New York

339. Complaint counsel do not claim, as the complaint alleges, that the acquisition will eliminate potential competition between Franzia and Coke-New York, but argue that these companies competed, before the acquisition, in the "all wine" market and that the acquisition eliminated that competition. [99]

340. The record does not support that claim. With minor exceptions,[42] Coke-New York's wines did not and do not compete with

[41] Mr. Ivie of Guild Wineries disagreed with this consensus, testifying that since the acquisition Franzia has tended, within particular (unnamed) price categories, to a higher price policy (Tr. 585).

[42] Tribuno and Franzia vermouths and, perhaps, the new Mogen David light wines and Franzia table wines. The significance of this competitive overlap cannot, however, be determined on this record.

Franzia's wines (Findings 212–237), and the acquisition did not and will not eliminate substantial competition between these companies.

III. Conclusions of Law

A. Coke-New York's Acquisition of Franzia Was Not Horizontal

Although a few witnesses agreed that all wines compete to some extent, most, whether called by complaint counsel or Coke-New York, expressed no concern about Mogen David's activities[43] because they simply do not view it as a competitor.

Complaint counsel answer that while producer testimony and other record evidence might require a finding that well-defined submarkets exist in the wine industry,[44] these submarkets "are not a basis **[100]** for the disregard of a broader line of commerce that has economic significance." *United States* v. *Phillipsburg Nat'l Bank,* 399 U.S. 350, 360 (1970).

Coke-New York does not disagree with the concept that relevant submarkets can exist within a broader line of commerce which is also economically significant, but it argues that there is no line of commerce in the wine industry which encompasses both Mogen David's and Franzia's wines. I agree: Complaint counsel's "all wine" market is a theoretical construction which does not take into account "the realities of the market in which the merged companies operate," *General Foods Corp.,* 69 F.T.C. 380, 408 (1966), *aff'd,* 386 F.2d 936 (3d Cir. 1967), *cert. denied,* 391 U.S. 919 (1968).

Coke-New York points out that *Brown Shoe* was not the first important case which defined how the limits of a relevant product market should be determined. The principal pre-*Brown Shoe* case, *United States* v. *E. I. Du Pont de Nemours & Co.,* 351 U.S. 377 (1956) (the *Cellophane* case), stated that in determining whether products are part of the same market

> What is called for is an appraisal of the "cross-elasticity" of demand in the trade. The varying circumstances of each case determine the result. In considering what is the relevant market for determining the control of price and competition, no more definite rule can be declared than that commodities reasonably interchangeable by

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[43] With the exception, of course, of the few producers of directly competitive wines such as Manischewitz (Finding 213).

[44] *Brown Shoe Co.* v. *United States,* 370 U.S. 294, 325 (1962):

> The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it. However, within this broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes. The boundaries of such a submarket may be determined by examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors.

consumers for the same purposes make up that part of trade or commerce, ... 351 U.S. at 394–95.

Do consumers believe that Franzia and Mogen David wines are interchangeable for the same purpose? Complaint counsel say that both are table wines, but there **[101]** is no reliable evidence of consumer belief that the sweet Mogen David wines with the "foxy" taste (Finding 223) are reasonable substitutes for table wines, dessert wines, or sparkling wines of the kind which Franzia produces.

Testimony by industry members provides secondhand but convincing evidence that consumers do not consider Franzia and Mogen David wines as interchangeable for the same purpose, for if this were so, surely wine producers and wine retailers would have realized this over the years and adjusted their business practices to take Mogen David wines into account.[45] Yet, while producers are concerned with the prices of many varieties of wine, they are simply not interested in the prices of Mogen David wines (Findings 229–232).

Logic also leads to the conclusion that Franzia's and Mogen David's wines do not exist in the same product market. The differences between Franzia's (and other producer's) table wines and Mogen David's wines are so pronounced (Findings 223–228) that it is inconceivable that a drinker of table wines would consider Mogen David wines a reasonable substitute for them.[46]

It is possible, of course, that young wine drinkers who initially began drinking pop wines or Mogen David traditional wines might move up to table wines (Finding 235) but this does not, I believe, indicate cross-elasticity of demand between Mogen David wines and table wines; rather, this shows that the wines are so different that they are unsuited for the same purpose, and that they are not substitutes for one another, see *du Pont, supra* at 393. **[102]**

Despite the evidence discussed above, complaint counsel say that "wine is wine," just as "beer is beer," *United States* v. *Jos. Schlitz Brewing Co.,* 253 F. Supp. 129 (N.D. Cal.), *aff'd per curiam,* 385 U.S. 37 (1966), and "dog food is dog food," *Liggett & Myers, Inc.* v. *FTC,* 567 F.2d 1273 (4th Cir. 1977). These cases can be distinguished from the present one. In *Schlitz,* the court could find no:

rational way of choosing a point along this price spectrum [of beer prices ranging from $.79 to $1.44 a six pack] and saying that all beer which sells above that point constitutes a line of commerce, or even a sub-market, apart from all beer which sells below that point. *Schlitz* at 145.

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[45] In other words, they would have recognized the cross-elasticity of demand between the products. *United States* v. *The Federal Co.,* 403 F. Supp. 161, 163 (W.D. Tenn. 1975).

[46] The studies which complaint counsel introduced in evidence do not, in my opinion, contradict this conclusion for they do not reveal the unfettered choices of even those who were interviewed (see Respondent's Post-Trial Reply Memorandum, pp. 27–29).

In other words, the court concluded that there must be an overall beer market since there were no clearly identifiable submarkets. Here there is no doubt that Franzia and Mogen David wines occupy separate submarkets; the question is whether they also compete in a broader market.

Liggett & Myers does not dictate the adoption of complaint counsel's "all wine" market. In this case, the Commission found the existence of an "all dog food market" because all dog foods, "including Perk's 'Economy' canned and Allen's 'premium' canned, is interchangeable for the same use-keeping dogs fed," because of the elasticity of dog food production facilities, and because of "substantial competitive confrontation among all members of the dog food industry. . . ." *Liggett & Myers, Inc.,* 87 F.T.C. 1074, 1148, 1153 (1976).

To state the obvious: Wine is different than dog food. In *Liggett & Myers,* despite distinct differences between premium and economy canned dog food, the Commission could not

> believe, that were a "premium" canned dog food unavailable, that even the most loyal of "premium" users would let their dogs starve rather than use an "economy" canned dog food. . . . *Id.* at 1157.

[103] On this record, it can be stated with confidence that the host of a dinner party, faced with the wide variety of table wines available to him, would almost certainly not consider any of the Mogen David traditional wines suitable to be served at his table.

Complaint counsel argue, however, that one cannot simply look at present attitudes of wine drinkers, but that competition must be viewed historically just as in *United States* v. *Continental Can Co.,* 378 U.S. 441 (1964), where the Supreme Court concluded that despite their distinctive characteristics, metal and glass containers occupied the same product market because of the historic confrontation between them in which "metal has replaced glass and glass has replaced metal. . .for some important uses; both are used for other purposes; each is trying to expand its share of the market at the expense of the other; and each is attempting to preempt for itself every use for which its product is physically suitable . . . ." *Id.* at 453.[47]

Over the past years, there has been a substantial increase in the sales of dry wines and a decrease in the sales of dessert wines (Finding 233) so that it can be said that there has been broad competitive confrontation between these groups of wines. However,

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[47] See also *Liggett & Myers, supra* at 1148:

> . . .competition should be viewed dynamically, and measured over a sensible period of time.

there is no mutual competition between the Mogen David and Franzia-type wines. Producers of Franzia-type wines are not trying to expand their wine sales at the expense of Mogen David wines. Their competitive activity is focused elsewhere. And, despite some half hearted attempts to convince others that it was a producer of table wines (Finding 202), Mogen David did not try to compete in the table wine market with its traditional sweet wines.[48] **[104]**

All of the evidence discussed up to now relates to the "demand side" of the relevant market. However, "cross-elasticity of production facilities may also be an important factor in defining a product market. . . ." *Brown Shoe, supra* at 325 n. 42. A "supply side" or "supply space" analysis recognizes "the ability of modern corporations to transfer their management, manufacturing, and marketing skills to related but unidentical product markets where profit opportunities beckon." *Sterling Drug, Inc.,* 80 F.T.C. 477, 587 (1972).

Coke-New York agrees that products which may not be directly competitive may nevertheless be included in the same relevant market under the so-called "cluster" concept, see *United States* v. *Philadelphia National Bank,* 374 U.S. 321 (1963), and concedes that conventional wines occupy a "cluster" composed of producers who compete with one another by offering a broad line of products which may not be directly competitive, such as sherry, burgundy and champagne. Coke-New York argues, however, that Mogen David wines are not in the same "cluster" as the products of conventional wine producers.

I agree with this argument. Despite the great variety of products which a conventional wine producer like Franzia sells (Finding 178), only one, Gibson, produces conventional wines as well as Mogen David-Manischewitz type wines (Finding 232). Every other conventional wine producer avoids these wines, and it would be unrealistic to include them in the conventional wine "cluster." Compare *British Oxygen Co., Ltd,* 86 F.T.C. 1241, 1369 (1975):

> On appeal complaint counsel seek to bolster the ALJ's finding on the ground that inhalation anesthetic equipment is a "cluster" market. . . . But as we pointed out in *Sterling Drug, Inc.,* . . . in "those cases it was established or undisputed that resource flexibility existed or that the product groupings were sold as a full line by most firms."

Nor is there "resource flexibility" between the producers of Franzia-type wines and Mogen David-type wines since Mogen David wines cannot legally be made in California where Franzia's facilities are located (Finding **[105]** 38), and Mogen David would hardly try to

[48] If its traditional wines were truly competitive with dry table wines, Mogen David would have perceived no need to produce its "light" wines (Finding 168).

produce Franzia-type table wines in its plants for they could not be called "California" wines.[49] However, even if one were to conclude that Mogen David and Franzia wines occupy the same "supply space," there is no evidence of the extent of that space, see *Sterling, supra* at 596, and, consequently, no way to determine Franzia's and Mogen David's share of that space.

Complaint counsel argue that Mogen David and Franzia are competitors because they vie for distribution, *Sterling Drug, supra* at 592; *A.G. Spalding & Bros. Inc.* v. *FTC,* 301 F.2d 585, 603–04 (3d Cir. 1962); *Litton Industries, Inc.,* 82 F.T.C. 793, 998 (1973); retail outlets, *Sterling, supra* at 583; and advertising, *Continental Can, supra* at 450–51. The answer to this argument is that these facts were considered in the cited cases along with other evidence of substantial competitive confrontation. Thus, despite theoretical "competition" for distributors, or shelf space,[50] all the evidence of record leads to the conclusion that there was no "meaningful competition" between Coke-New York and Franzia before the acquisition, and that the acquisition did not, therefore, eliminate actual competition between these companies.

B. Even if the Acquisition Were Horizontal, It Would Not Substantially Lessen Competition

Although I have found that the Coke-New York Franzia merger was not horizontal, I will comment on complaint counsel's and Coke-New York's arguments on the combined market shares of the two companies. [106]

Its 1973 acquisition of Franzia made Coke-New York the nation's third largest wine producer, with 7.17 percent of a market in which the top four firms in the prior years had 55 percent and the top eight had 65 percent of the wine gallonage. Complaint counsel argue that these facts coupled with the increase, over the five years prior to the acquisition, of the four and eight firm concentration ratios by 8 and 10 percentage points makes extensive analysis of the wine market unnecessary. *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 363 (1963).

However, the marked share figures and concentration ratios are not, in my opinion, so impressive that one can ignore other facts, including post-acquisition evidence, which may lead to a conclusion contrary to that which the numbers might appear to dictate. See

[49] Canandaigua, a producer of New York State table wines which are competitive with California table wines, nevertheless bought a California winery so that it could produce California wines (Finding 226).

[50] Theoretical, because if one were to accept complaint counsel's argument, every product in a grocery store which sells wine could be considered a competitor of wine.

Sterling Drug, Inc., supra at 598; *United States* v. *International Harvester Co.,* 564 F.2d 769, 773 (7th Cir. 1977).

Despite the obvious limitations of post-acquisition evidence, it is admissible and can be considered "in exceptional circumstances," *American General Insurance Co.,* 89 F.T.C. 557, 632–33 (1977). In *Warner-Lambert Co.,* 87 F.T.C. 812 (1976), the Commission "while not suggesting that the presence of post-merger market share data is necessary in merger cases" considered it because it corroborated projections based on premerger market share data. *Id.* at 868, n. 11. See also *United Brands Co.,* 83 F.T.C. 1614, 1712–14 (1971), in which the Commission relied on post-acquisition evidence of the failure of that company to successfully brand differentiate lettuce.

Although I agree that "the force of § 7 is still in probabilities, and not in what later transpired," *Seeburg Corp.,* 75 F.T.C. 651, 665 (1969), I cannot ignore the post-acquisition evidence tendered by Coke-New York for it reveals that the trends predicted in the complaint are nowhere near as significant as complaint counsel contend.

While concentration ratios increased substantially in the four years preceding the merger, the top four increase was only 0.67 percent from 1970 to 1976 (Finding 245). This evidence (which includes both pre- and post-acquisition figures) reveals that at present there is no discernible trend toward concentration. Furthermore, the market shares of three of the top four wine producers have [107] declined over the past several years. In fact, from 1974 to 1977 Coke-New York's share of the wine market decreased from 6.35 percent to 4.72 percent (Finding 242). Nor can Franzia's losses—$11.6 million—in the past four years be ignored (Finding 189) or its presence in the private label market, which is totally price competitive (Findings 74–75); however, the most significant fact which indicates that the market share data in the record does not reflect the actual state of competition between the companies is Mogen David's absence from New York and California, the two largest wine consuming states, and, therefore, the lack of direct competitive confrontation between it and Franzia in these states[51] (Findings 162, 336). See *Warner-Lambert, supra* at 914; *United States* v. *Federal Co.,* 403 F. Supp. 161 (W.D. Tenn. 1975):

At the time of the acquisition, Federal and White Lily were less significant competitors of each other in the bakery flour market in the Southeast and in

[51] It is not inconsistent, as complaint counsel claim, to accept the parties' agreement that the relevant geographic market is nationwide and, at the same time, to recognize that Franzia and Mogen David do not compete in every geographic submarket across the United States.

plaintiff's proposed four-state area than the foregoing market share figures would indicate. *Id.* at 169.

If Mogen David and Franzia are viewed as competitors under a "cluster" or "supply side" analysis, it is important, I believe, to recognize that even in those states where both are selling their wines, they are not in direct competition for the same consumer dollar as are companies producing table wines, another fact which diminishes the significance of the market share data relied upon by complaint counsel.

Finally, the entry of an important new competitor, Bronco, and other wineries (Findings 302–318) shows that there are no substantial monetary barriers to entry in **[108]** the wine business.[52] Know-how is of course important, but it can be easily bought. Compare *United Brands Co., supra* at 1708–09.

Thus, the market share data relied upon by complaint counsel does not tell the whose picture. The acquisition did produce a company which is the third largest in the industry, but its market share has declined steadily since then, the acquired company has lost over 11 million dollars,[53] the industry is not tending toward concentration, complaint counsel make to claim that there is a trend toward acquisitions in the industry, there has been significant new entry which has apparently adversely affected the market shares of three of the top four producers, popular priced wines are competitively priced in non-control states[54] (Findings 67–77), and producers' profits are low (Finding 69). In conclusion, wine is a competitive industry, and there is no evidence that the acquisition has changed or will change this condition.

There have been horizontal mergers which were declared illegal where the market shares were close to those here (7.17 percent at the time of the acquisition, 4.72 percent as of 1977), but the merged companies in those cases operated in a different competitive environment than exists in the wine industry. **[109]**

In *United States* v. *Pabst Brewing Company,* 384 U.S. 546 (1966), Pabst, the tenth largest brewer, acquired Blatz Brewing. Although the combination controlled only 4.49 percent of the total sales of the industry nationally at the time of the acquisition, the two companies were head-to-head competitors and the beer industry was one

[52] In *Fruehauf Corp.,* CCH Trade Reg. Rep. Trans. Binder § 21,402, at 21,368 (February 22, 1978), the Commission described costs of entry into the ASBD market of up to 13 to 14.6 million dollars as moderately high. Significant entry in the wine industry has been accomplished for much less (Findings 306, 324).

[53] *United States* v. *International Harvester Co., supra* at 769, 773 (7th Cir. 1977):

> In responding to a statistical showing of concentration and in concluding that Section 7 was not violated, Judge Leighton properly considered evidence of Steiger's "weakness as a competitor."

[54] A "reliable indicator of desirable market behavior." *United States* v. *Black & Decker,* 430 F. Supp. 729, 754 (D. Md. 1976).

marked by a steep decline in the number of competitors (from 206 to 162 in four years). The Court also found high entry barriers in the beer business and a substantial increase in concentration in the market. Furthermore, the Court placed great emphasis on the fact that Pabst's market share grew in the three years following the merger. 384 U.S. at 550–51.

In *United States* v. *Von's Grocery Co.,* 384 U.S. 270 (1966), the combined market share of a union between two retail grocery chains was only 7.5 percent in the year after the acquisition. However, it was also clear that the Los Angeles retail grocery market was experiencing a severe decline in the number of independent grocery stores, which were rapidly being acquired by chain operations, and the two merging companies were growing, successful and in direct confrontation in the marketplace.

While post-acquisition evidence should be considered with care, it would be unrealistic to ignore the convincing, consistent picture which that evidence discloses in this case. On the basis of that evidence, even assuming that Mogen David and Franzia were in the same product market prior to the acquisition, I find that complaint counsel have not established that the effect of the acquisition may be to substantially lessen competition.

C. The Acquisition Viewed as a Product Extension

Coke-New York's acquisition of Franzia was not horizontal; it was, rather, a product extension acquisition, one involving the "merger of sellers of functionally closely related products which are not, however, close substitutes." *The Procter & Gamble Co.,* 63 F.T.C. 1465 (1963), *aff'd,* 386 U.S. 568 (1967). **[110]**

The Supreme Court in *Procter, supra* at 578, outlined the anticompetitive effects of product-extension mergers:

> (1) the substitution of the powerful acquiring firm for the smaller, but already dominant, firm may substantially reduce the competitive structure of the industry by raising entry barriers and by dissuading the smaller firms from aggressively competing;
>
> (2) the acquisition eliminates the potential competition of the acquiring firm.

Complaint counsel have abandoned any claim that Coke-New York was a potential entrant into table, dessert and sparkling wines, so the only issue to be dealt with is the effect of the substitution of Coke-New York for Franzia.

Of major importance in a product-extension acquisition is the probability that it will permit "significant integration in the production, distribution or marketing activities of the merging firms," including the combination of advertising and sales promotion activities. *Procter & Gamble, supra,* 63 F.T.C. 1543.

Significant integration may substantially lessen competition by entrenching an already dominant firm, *Procter & Gamble, supra* at 1568, or by upsetting the competitive balance in an industry, *General Foods Corp.,* 69 F.T.C. 380, 422–23 (1966), *aff'd,* 386 F.2d 936 (3d Cir. 1967), *cert. denied,* 391 U.S. 919 (1968), or by increasing barriers to entry, *United Brands,* 83 F.T.C. 1614, 1706 (1974).

The present acquisition has none of the features of an illegal product extension merger. Although Franzia was one of the larger wine producers prior to the acquisition, it was not the dominant firm nor did it provide any competitive balance in the industry—Gallo was, and is, the dominant firm in this industry, although its market share has declined somewhat over the past few years. [111]

Furthermore, the ability to alter market structure through massive advertising—a common theme in product extension cases[55]—is not a factor in the wine market for, while advertising can contribute to a wine producer's success, it is not essential, and has even been dispensed with by some successful wineries (Findings 50–63). See *United States* v. *Crowell, Collier and Macmillan, Inc.,* 361 F. Supp. 983, 991–92 (S.D. N.Y. 1973):

> Advantage for § 7 purposes, however, means substantial competitive advantage. The ability of the smaller acquired firm to advertise at the rates enjoyed by its purchaser has been found injurious to competition only where advertising is itself a significant factor in the smaller firm's market.

Barriers to entry in the wine industry are low, they have been surmounted by new entrants in the popular priced field (Findings 302–332), and there is no convincing evidence that the Franzia acquisition will raise these barriers.[56]

Coke-New York denies that it will integrate Mogen David's and Franzia's sales forces or that it will be able to force distributors to take on all of its wine [112] products and drop those of other wine producers,[57] I agree that this possibility is remote, especially in view

[55] In *Sterling Drug, Inc.,* 80 F.T.C. 477, 540–41 (1972), the Commission was concerned with advertising to sales ratios ranging from 16 percent to 45 percent. In *General Foods Corp.,* 69 F.T.C. 380, 434 (1966), *aff'd,* 386 F.2d 936 (3d Cir. 1967), *cert. denied,* 391 U.S. 919 (1968), SOS had an advertising to sales ratio of over 15 percent. In *FTC* v. *Procter & Gamble Co.,* 386 U.S. 568, 571–72 (1967), Clorox had an advertising to sales ratio of over 9 percent in the year of the merger. In *Liggett & Myers, Inc.,* 87 F.T.C. 1074, 1117, 1174 (1976), *aff'd,* 567 F.2d 1273 (4th Cir. 1977), Alpo had an advertising to sales ratio of 10 percent.

[56] In a product extension acquisition, the key question is not so much what barriers to entry there are but "whether respondent's presence has in any way raised whatever . . . entry barriers existed prior to its acquisitions." *United Brands, supra* at 1706.

[57] While Mogen David would be expected to refrain from pressuring its distributors to take on Franzia during this litigation, if, as complaint counsel contend, Mogen David distributors feel obliged to do so even without overt coercion ("Coercion is often extremely subtle, especially economic coercion," CRF, p. 80), one would expect, over four years after the merger, that Franzia's sales would have increased substantially. They have not (Finding 192).

of its substantial recent decrease in market share (Findings 276-301). Furthermore, even assuming that many Mogen David distributors do take on Franzia's wines or that the Mogen David and Franzia sales forces are combined, this will not foreclose other wine producers from obtaining adequate distribution (Findings 91-161).

D. Conclusions

1. Coke-New York's acquisition of Franzia was not horizontal.
2. Assuming that Coke-New York's acquisition of Franzia was horizontal, complaint counsel have not proved that its effect may be substantially to lessen competition, or that it may tend to create a monopoly.
3. Coke-New York's acquisition of Franzia was a product extension, but complaint counsel have not proved that its effect may be substantially to lessen competition, or that it may tend to create a monopoly.

ORDER

It is ordered, That the complaint be, and it hereby is, dismissed.

OPINION OF THE COMMISSION

BY DIXON, *Commissioner:*

Complaint in this matter was issued on September 10, 1974, challenging the acquisition by Coca-Cola Bottling Company of New York, Inc. (hereinafter Coke-New York) of Franzia Bros. Winery, a producer of California table wines. Coke-New York had previously acquired the Mogen David Wine Co. in 1970 and the Tribuno Vermouth Co. in 1973. The combination of Franzia and Mogen David made Coke-New York the third largest factor in the wine industry, accounting for 7.17 percent by volume of domestically produced wine and imports for domestic consumption in 1973. By 1977, however, this figure had fallen to 4.72 percent. (I.D. 242)[1]

[2] Hearings on the complaint, which alleged a violation of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45) as well as Section 7 of the Clayton Act (15 U.S.C. 18) were held before Administrative Law Judge (ALJ) Lewis Parker, who entered an initial decision holding that the merger did not violate the law.

[1] The following abbreviations are used herein:

I.D.	- Initial Decision, Finding No.
I.D. p.	- Initial Decision, Page No.
Tr.	- Transcript of Testimony, Page No.
CX	- Complaint Counsel's Exhibit No.
RX	- Respondent's Exhibit No.

Judge Parker concluded that "all wine" did not constitute an appropriate line of commerce within which to evaluate the merger, but that even if it did, the merger had not been shown to threaten a substantial lessening of competition in that hypothetical market. Complaint counsel have appealed from both prongs of the ALJ's holding, and our disposition of this appeal follows.

RELEVANT MARKET

While complaint counsel contend that "all wine" is the relevant product market within which the effects of this merger are to be judged, respondent insists, and the ALJ agreed, that Mogen David and Franzia wines do not inhabit the same "line of commerce" within the meaning of Section 7. Respondent is apparently willing to concede that there exists a "wine market" of sorts, consisting of a cluster of products among which fall dry table wines and sweeter dessert and aperitif wines, but it argues that Mogen David cannot fairly be included within any such market that might be defined. Instead, it is claimed, Mogen David occupies its own "quiet corner of the alcoholic beverage business" in which it competes with Manischewitz and a few other berry wines for the patronage of people who "are not really wine drinkers" (Respondent's Answer Brief, pp. 2, 10; Tr. 2229).

On the surface, this proposition appears implausible. After all, Mogen David is called "wine"; is thought by those who produce and advertise it to be wine and to compete with many other wines; is distributed by the same class of specialized vendors who distribute other wines; occupies shelf space in retail liquor stores along with other wines; is counted among "wine" sales in industry statistics; contains 12 percent alcohol; is made from the crushed and fermented fruit of the vine; and, if consumed in sufficient quantities will (we presume) produce a state of intoxication roughly equal to that induced by the best or worst offerings of California or France. Why, then, is this wine different from all other wines? [3]

In respondent's view, the answer to our question lies in Mogen David's high added sugar content, which makes it considerably sweeter than all but the competing products of Manischewitz and a few others. This assures, in respondent's view, that Mogen David will be consumed by an entirely different and separate class of customers from those who purchase Franzia or other table wines. Respondent does not go quite so far as to suggest that the sophisticated dinner party host(ess) would sooner abandon his or her guests to an evening of unremittingly sober contemplation of each other's conversation than ply them with Mogen David, but it is certainly the thrust of respondent's argument that in the unlikely event that a Franzia drinker were to be confronted with that frightful possibility, he or she would as readily turn for relief to beer or whiskey as to Mogen David.[2] In other words, it is alleged, the cross-elasticity of demand between Mogen David and Franzia (or similar wines) is zero, a point made in not so many words by several hardly disinterested fanciers of California table wines who testified that neither they nor any true oenophilist would drink Mogen David if it were being given away, (Tr. 461, 915, 1089), or, even (according to one witness) if he were paid one dollar a glass to drink it (Tr. 462).

Following up on this point, respondent's counsel have gleefully elicited from the witnesses in this case any number of fervent denunciations of Mogen David's claim to occupy the same market as California table wines. Thus, as one witness observed, "[t]hey make grape alcohol that has sugar and water added. We make wine." (Tr. 915) In the view of another, Mogen David's MD 2020 is "a harsh, syrupy tasting, heavy alcohol, raspy, difficult to even smell, let alone get over your palate, type product." (Tr. 1008) And, of course, there is the gentleman who, badgered by counsel for his evaluation of the taste of "eastern grapes" responded with that "rather earthy" characterization that Judge Parker apparently considered too earthy even [4] for the calloused sensibilities of the antitrust bar.[3] (Tr. 311, I.D. 223; *see also* Tr. 1914–15, 2044, 2117, 2160).

While these descriptions of Mogen David, elicited by its own counsel, might, in a sense transcending this litigation, be considered "admissions against interest," we are reluctant to accept them at face value. Those who consume this product may number among them few members of the wine-drinking elite, but it seems apparent that Mogen David is consumed for general light, medium, or heavy duty libationary purposes by a wide spectrum of Americans whose dollars are capable of exerting quite as much influence in the market for wine as anyone else's.

Although many of Mogen David's products are kosher, and, therefore, suitable for celebrations of the Jewish religion, it is quite clear from the record that only a minority, and perhaps a small minority of the purchasers of Mogen David (and Manischewitz) are Jewish. This was the purport of testimony from several sources (*e.g.,* Tr. 1328, 1437, CX 52–Z–144–45) and respondent introduced no

[2] Indeed, respondent goes farther: "Mogen David drinkers don't drink wine. The wine drinker surely doesn't drink Mogen David. It is not a question of price or anything else. If you are a regular drinker of California wines, you would not switch to Mogen David if they paid a half dollar a glass to drink it. You would rather go to Coca-Cola." (Tr. 15) While this admission on the part of counsel for Coca-Cola Bottling Co. does raise the interesting possibility of other relevant markets within which the acquisition might have been tested, complaint counsel have not chosen to pursue them.

[3] This Commission will not abridge the protections of scatological privilege either. (But it rhymes with "sissy.")

evidence to contradict it. Indeed, Mogen David seeks patronage well beyond the Jewish community (I.D. pp. 59–61) and Mogen David reports that its best sales season is, as it is for other wines, the fourth quarter of the year (CX 52–Z–18; cf. Tr. 1464). Thus, even assuming that Jewish purchasers of Mogen David drink it solely for religious reasons,[4] a proposition that itself seems unlikely, it is nevertheless clear that the bulk of Mogen David is consumed for the same set of reasons that motivate the consumption of all other wines.

Respondent contends, nevertheless, that those who drink Mogen David are an altogether different group from those who drink California table wines, and that the latter are unlikely to purchase Mogen David [unless, perhaps, as one witness explained, "they are bringing it home to their old mother or aunt or somebody like that." (Tr. 2083)]. Noting that, as their taste matures, wine drinkers typically develop [5] a preference for drier, less sweet wines, respondent suggests that the disparity in sweetness between Mogen David and the cluster of products produced by Franzia is so great that at any particular point in an individual's drinking career, he or she is unlikely to alternate between wines of the two companies. Mogen David, then, is at best for the youthful drinker, aged 18–21 or 10–15 (depending upon whether one reads the statute books or the newspapers) whose transition to the role of mature tippler is eased by the sugar in Mogen David but who, upon achieving that status, quickly renounces the medium that made it all possible. (Tr. 1327, 1374, 1407–08, 1446, 1458–9, 1504, 2301). Mogen David, it is suggested, is also of special appeal to lower income minority groups (Tr. 1574, 1852, 1981) as well as to older Americans of all races and creeds who have never "dried up."[5] (Tr. 1982, 2083, 2116)

One large retailer described the non-Jewish purchasers of Mogen David as being

> . . .either black, poor black, poor Spanish or Puerto Rican or else they are older people. A lot of times old ladies will come in and say they have been at the doctor and have an artery problem and the doctor recommended drinking a little bit of wine everyday and ordinarily, they don't drink wine, they want something. . . (Tr. 2102)

Following up on the testimony, respondent suggests that the reason for Mogen David's recent precipitous loss of market share lies in the fact that its customers are "just getting older and not drinking any more, dying." (Oral Argument Transcript, p. 51)

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[4] There is no suggestion in the record that Mogen David would find any substantial use as a sacramental wine in the Christian religion, and, in fact, its high sugar content apparently renders it unsuitable for rites of the Catholic church. (Tr. 1329).

[5] "Drying up" (not to be confused with its opposite, "drying out") is the process whereby wine drinkers gradually shift from sweet to dry wines. (Tr. 2289)

While this orgy of casual empiricism may point in the direction of truth, it does not negate the existence of significant areas of competitive confrontation between Mogen David and a variety of other wines. Youthful drinkers, for example, do not make the transition from sweet to dry wines with the same abruptness and finality as they progress, for example, from elementary school to junior high. Rather, there is a period during which experimentation [6] occurs, different wines are tried, and brands are alternated. Many witnesses, including some who expressly denied that Mogen David competed with Franzia or other California wines, acknowledged that all wines (sometimes expressly mentioning Mogen David) compete for the patronage of the fledgling drinker. (*e.g.,* Tr. 1092, 1327, 1504–08, 2301, I.D. 235).[6]

Moreover, other evidence of record, in particular marketing studies commissioned by Mogen David to assist it in selling its products suggests that (1) Mogen David is considered by those who use it to be suitable for consumption at mealtimes, and (2) some of those who consume Mogen David also enjoy and consume a variety of other sweet and dry wine products. Thus, Mogen David's surveyor, who contacted a sample of 420 wine drinkers in four cities, reported that 84 percent of those 150 who claimed to "prefer" Mogen David; 77 percent of those 144 who simply "used" Mogen David; and 70 percent of those 126 who "know but don't use" Mogen David considered it suitable for consumption with a meal. (CX 737 X). Asked to state the time they most commonly served sweet wine, 49 percent of Mogen David preferrers responded that it would be at dinnertime, while another 27 percent said they would be most likely to serve it equally at dinnertime or after or before the meal. (CX 737 X). When asked as to their preferences in wine taste, 27 percent of the Mogen David "preferrers" indicated that they preferred dry wines, while 46 percent preferred sweet wines. 43 percent of the Mogen David "users" in the sample preferred dry wines, compared to 37 percent preferring sweet wines. (CX 737 W). Finally, the study revealed that when choosing an alternative to Mogen David, 11 percent of the Mogen David preferrers would turn to Italian Swiss Colony and 16 percent to Gallo, while 33 percent would turn to Manischewitz. (CS 737 Z–80). Among the Mogen David preferrers,

[6] In a move aimed at the youth market, Mogen David developed Cold Bear, a non-kosher pop wine. (CX 17 V ff.) Like other pop wines, this product met some initial success but later fizzled. (I.D. 166) Of more sustained significance has been MD 20 20 (modestly subtitled "The wine of the century"), also non-kosher, and "targeted initially to ethnic market" where there had been "inactive competition" and "no recent new product activity" (CX 17 U). MD 20 20 has been a highly successful product (Tr. 1008), and appears to have particular appeal to black consumers, (Tr. 1981) and to young consumers. (Tr. 2271) By 1972 it accounted for 50 percent of Mogen David's sales (I.D. 169).

Gallo was rated the first or second alternative by 33 percent and Italian Swiss Colony by 24 percent. (CX 737 Z-81). [7]

Although respondent attacks this survey as being unsuitable for the use to which complaint counsel seek to put it, and not projectible to the population at large, we believe that the survey results are plainly probative of points at issue in this litigation. It is true, as its author conceded, that the survey is not projectible, and we, therefore, would not rely on the particular percentages cited above as being accurate for the entire all-wine or Mogen David drinking population. Nevertheless, the survey does represent by far the most systematic canvass of consumer attitudes available in the record. While these results are not projectible to any entire population, they surely reflect the attitudes of a significant segment of such population. No stronger claim than this could possibly be made for the contrary, anecdotal evidence cited by respondent. Thus, it may be that the three wine retailers who testified in this case have rarely if ever seen a Mogen David buyer approach the cash register with anything but Mogen David in their cart, but the "testimony" of hundreds of consumers reflected in the survey does suggest that such occurrences, aberrant as they may seem, may not be uncommon. Similarly, though the wine industry executives who testified at these hearings might find it an appalling breach of good taste, it nonetheless seems plain that large numbers of Mogen David drinkers consider the product to be a quite suitable accompaniment to a meal. Indeed, it is hard to imagine how else Mogen David could have sold up to 14 million gallons of its wines yearly (I.D. 170) if their use was so limited as many of the witnesses appear to believe.

Given the foregoing testimonial evidence of competitive confrontation between Mogen David and other brands for patronage of the new drinker, and given more modest survey evidence suggesting some competition with other non-kosher wines for patronage of the general drinker, we think that the record demonstrates at least some significant competitive overlap or interchangeability of end use between Mogen David and other wines. To be sure, significant competitive confrontation between Mogen David and many other wines at the other end of the sweetness spectrum is probably minimal. But Mogen David is not unique in this respect. Many of the witnesses who testified in this proceeding that their companies' products do not compete with Mogen David, also excluded from the realm of their competition a wide range of other wines that clearly belong in any sensibly defined "wine [8] market." Thus, one witness even doubted that red wine competed with white (Tr. 2171), but more generally, industry members saw the bulk of their competition as

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coming from similar type wines within a narrow price range. Asked to describe his product's competitive interface with Gallo, one manufacturer of premium wines responded:

I prefer to think of Gallo as the wine they drink everyday. At least I hope to think of Gallo as the wine people drink everyday and people might buy ours to drink on Sundays. (Tr. 2181)

In the words of another:

The average dry wine consumer, and I would lump basically all the dry wines would tend to float from say, maybe a low priced level as a general rule to a little bit higher level as a special occasion or weekend type thing. (Tr. 2228; *See also* Tr. 2036).

These industry members appear to view wines in different price categories as being in some measure *complements* rather than substitutes for each other, and in some measure they no doubt are, just as a wine like Mogen David might be consumed by the same person but for a different purpose than would a drier wine. All this, however, illustrates only that the wine market does not consist of altogether homogeneous products. Many wines may be both substitutes and complements for each other,[7] and as between many market members, cross-elasticity of demand may be slight. The products in the alleged market, however, can be arrayed along a set of continua, most significantly price and sweetness, and while Mogen David plainly falls at the far end of the latter continuum, we see no clear reason why it should be excluded from that continuum altogether, given clear interchangeability of end use with some products nearer the center, cf. *United States* v. *Jos. Schlitz Brewing Co.*, 253 F. Supp. 129, 145 (N.D. Cal.), *aff'd. per curiam*, 385 U.S. 37 (1966). [9]

While evidence of interchangeability of end use may be the most important determinant of the existence of a market, cf. *United States* v. *E. I. du Pont de Nemours & Co.*, 351 U.S. 377, 394–5 (1956), it is not the only one, *Brown Shoe Co.* v. *United States*, 370 U.S. 294, 325 (1962). Supply side flexibility is also an important factor, *Brown Shoe Co.* v. *United States, supra*, 370 U.S. at 325, n. 42, and in this regard the law judge observed that most of the equipment used for making wine "can be used interchangeably no matter what the specific wine

[7] As a further example, consider table wines consumed with dinner, and sweeter dessert or aperitif wines consumed after or before a meal. The compleat dinner party host(ess) may consider it imperative to stock all three, but the couple without guests may find that a few drinks before dinner coupled with the prospect of a few with dessert obviates the need to open a new bottle with the meal. Alternatively, the sight of a fine bottle of burgundy breathing on the dinner table may deter the consumption of aperitifs (or then again, it may not.)

type. Thus, most large wineries can produce any type of wine, even kosher wine, if the grapes are available." (I.D. 37)[8] While California law would preclude Franzia from adding sugar to a wine, (I.D. 38), it and other California producers could make very sweet wines by use of grape concentrate. And Mogen David's facilities could certainly be used (as they have been before) for manufacturing dry table wines of the sort made by California or New York wineries.[9] It does not denigrate the significance of this supply side flexibility to point out that Mogen David has had little success with its line of dry wines. Under other circumstances (*e.g.*, a decline in the number of competing brands) it might fare better, and have greater incentive to try, unless, of course, it should happen to own a competing seller of such wines. One possible effect of any merger involving companies with interchangeable manufacturing facilities is that it will stifle the incentive for product innovation by those firms in the best position to provide it. **[10]**

For the foregoing reasons, we believe that "all wines" might appropriately be designated as a market within which the effects of this merger may be tested. To be sure, the question is, as Judge Parker recognized, a close one, and were we disposed to reach a different conclusion with regard to the second issue in this case, the probable effects of the merger, we might well remand with respect to the question of market definition, perhaps for brief further consideration by the ALJ of the validity of the marketing studies that he appears largely to have discounted. For present purposes, however, we shall simply vacate the ALJ's conclusion that no market exists and assume *arguendo* that all wine is an appropriate market within which to judge the effects of the merger.

COMPETITIVE EFFECTS OF THE MERGER

In proceeding from there to measure those effects, however, the character of the market selected cannot be ignored. The principles governing antitrust market definition are designed to satisfy the necessity to make difficult judgments in an area of unavoidably imperfect knowledge, and markets so designated cannot always (nor need they, as a matter of law) satisfy the purist's desire that every product within them possess a high and statistically demonstrable

[8] This commonality of production facilities is further intensified by a commonality of distribution facilities. "Wine products" are distributed by wine distributors. While beer distributors or others can sometimes perform the job, it seems clear that distributors with specialized capabilities for handling all wines are preferable. This gives a further advantage to the manufacturer of one wine seeking to switch production to a different wine.

[9] We do not understand the law judge's surmise that Mogen David would not dare to produce "Franzia type" wines because they could not be called "California" wines. (I.D. p. 105). Surely the outer boundaries of competition in this industry are not so confined as to exclude products made east of the Rockies (or east of the Atlantic Ocean) from the same broad market as California wines.

degree of cross-elasticity of demand with every other. But by the same token, this cannot be an excuse for ignoring entirely what may be the peculiar characteristics of the market that has been chosen to test a merger, and assuming that because it is properly deemed a "market" it has all the characteristics of more fully integrated lines of commerce. As we noted in *RSR Corp.*, 88 F.T.C. 800 (1976), *aff'd*, No. 77-1413 (9th Cir., Jan. 8, 1979), a case in which there was much to argue against designation of any particular geographic market:

What this suggests is not that it is impossible to designate an appropriate 'section of the country' for purposes of antitrust scrutiny but rather simply that designation of an appropriate market does not end the analysis and divest the Commission of an obligation to keep in mind the multifaceted character of the market in its analysis of anticompetitive effects." 88 F.T.C. at 886.

[11] The same is true with respect to product markets. While a merger that created a company with a market share equal to that present here might well tend substantially to lessen competition in many markets, the record generated in this case does not give us cause to fear such an effect from the combination of Franzia and Mogen David in the sale of all wines.

As complaint counsel recognize, the relatively small market shares of the two merging firms in this case are hardly sufficient, standing alone, to give rise to a presumption of anticompetitive effects, as in *United States* v. *Philadelphia National Bank*, 374 U.S. 321, 363 (1963). In the year of the merger, the consolidated market share of the parties was 7.17 percent on a gallonage basis. (I.D. 241)[10] The year of the merger marked the beginning of a precipitous decline in Coke-New York's wine fortunes. By 1977 its market share had fallen to 4.72 percent (I.D. 242), with the slide due in part to losses by Franzia but most significantly as the result of a steady erosion of Mogen David's sales, from over 14 million gallons in 1972 to only slightly more than 9.5 million by 1977. (I.D. 170) While we are mindful that post-acquisition evidence, including declines in market share, should be viewed with a jaundiced eye where it is within the power of the respondent to manipulate, *United Brands Co.*, 83 F.T.C. 1614, 1703 (1974), it is also clear that the series of calamities that has befallen Mogen David-Franzia since their merger (*e.g.*, I.D. 170, 189-93, 336-337) amounts to something considerably more than the "reasonable cynic" could ascribe to a desire to avoid an adjudication of liability in this litigation. In considering the combined market

[10] Coke-New York argues that this figure would be lower if dollar share of the market were considered, because Franzia sells at the low end of the wine price range while Mogen David is at best in the middle. We believe that both figures are of interest, and of relevance, but it is certainly not inappropriate to assign liability on the basis of gallonage.

shares of the parties, then, the 7.17 percent figure clearly overstates the case, although we would ordinarily look to the year of merger figure as the best estimate of combined market share.

In an effort to go beyond the relatively low market shares, complaint counsel have additionally argued that industry concentration is high and that the combination of [12] Mogen David-Franzia is likely to achieve certain marketplace advantages attributable only to size, rather than to competitive vigor.

With respect to industry concentration, it is assuredly high, due principally to the large market shares of the top two firms. Four firm concentration prior to the merger was 55 percent and eight firm concentration was 65 percent and these figures had been increasing before the merger occurred. (I.D. 243) High concentration may facilitate the occurrence of interdependent anticompetitive conduct, and accordingly, even small increases in highly concentrated markets must be viewed with great disfavor. *United States* v. *Philadelphia National Bank, supra,* 374 U.S. at 365, n.42; *Stanley Works* v. *FTC,* 469 F.2d 498, 504 (2d Cir. 1972), *cert. denied,* 412 U.S. 928 (1973). Such a concern in this instance, however, is mitigated by the fact that the particular merging companies are ones as to which there exists little overlap of end use between the products they manufacture, and accordingly, the likelihood that this merger will increase opportunities for interdependent behavior on the selling side appears remote. Given their disparity of product offerings neither Mogen David nor Franzia seems likely to forfeit significant independence of action because of joinder with the other. This situation contrasts sharply with those in *United States* v. *Aluminum Co. of America,* 377 U.S. 271 (1964), and *Stanley Works* v. *FTC, supra,* both of which involved mergers of very small firms with leading firms in highly concentrated industries. In both of these cases, the mergers under challenge involved the presumptive loss of a fairly direct competitor of the industry leaders. In a concentrated industry, even the loss of such a small competitor is to be prevented. Here, however, we cannot conclude that either Franzia or Mogen David has been "lost" to the industry in any practical sense, because the extremely disparate nature of their product lines ensures that it is in Coke-New York's long term economic interest that both continue to compete vigorously in the sale of the line of products in which each specializes.[11]

[13] Complaint counsel have also pointed to the possibility that by

[11] This is, of course, the promise that is held out by the respondent in most merger cases, and ordinarily we would give it little credence. This case is different from most other cases, however, in that the merging parties, though perhaps assimilable within the same market, are the most diverse imaginable participants in that market, with little actual or likely market overlap.

virtue of its combination with Mogen David, Franzia will be "leveraged" into Mogen David distribution outlets to which it might not otherwise have been able to obtain access. There is record evidence to suggest that, at some level at least, a wine company's size is a determinant of the quality of distribution it is able to achieve. There is no doubt from the record that in many instances, the talent or market clout of wine distributors is critical to the competitive success of particular brands. To be sure, this is not always so. Where a brand is well known, perhaps as the result of nationwide advertising, it may be of relatively little significance who is chosen to distribute it, and all distributors will be eager to do so. (Tr. 1057) In other instances, however, it is clearly the distributor who is responsible for the success of a brand. (Tr. 257) In competing for distribution, size can be an advantage. A distributor may prefer to handle the line of a large company because it affords a readily available "mix" of complementary products (Tr. 1039, 1862), or, a distributor may feel compelled to handle the less desirable products of a larger company in order to be assured of being able to handle its more popular brands. (Tr. 950) The result of these tendencies, combined with an alleged preference for exclusivity in distribution (Tr. 1057), it is suggested, is an arrangement in which the biggest or best wine manufacturer preempts the most desired distributor in an area, the second largest obtains the second-best, and so forth. (Tr. 9–10, 117.)

Applying these observations to the instant merger, complaint counsel argue that it raises the substantial possibility that Franzia wines will be leveraged into the Houses of Mogen David, with distributors who might otherwise prefer to distribute competing brands of California table wines being compelled — or at least feeling compelled — to distribute Franzia in order to maintain their standing vis-a-vis Mogen David. While this phenomenon, if shown to exist in substantial degree, would be a cause for substantial concern, we find the record evidence on the point to be inconclusive.

Mogen David-Franzia clearly runs a very distant third (if not, by now, fourth) to the industry leaders, Gallo and United Vintners. (I.D. 241–42) While the ability to use leverage in the fashion feared by complaint counsel may be significant with respect to companies with larger market shares, it appears to be considerably less with respect to a [14] company of the size and with the product mix of Coke-New York. One reflection of this is the fact that a large fraction of Mogen David's distributors also distribute Gallo (Tr. 950), an arrangement that appears to work well for all parties because of the minimal overlap between the two lines. However, Gallo distributors are unlikely to be eager to add Franzia to their line, or if they do add it, they are unlikely to do an energetic job of promoting it because of its substantial overlap with Gallo. This, in turn, suggests that the only likely casualty of consolidation in such houses will be Franzia. (I.D. 292–98)

Because of difficulties and lack of success experienced in consolidation, Coke-New York re-separated the sales organizations of Mogen David and Franzia. (I.D. 300) While such a post-complaint occurrence, readily within the control of respondent, is no grounds to presume that further efforts at consolidation may not be made after the merger, we do not find substantial record evidence to fear that this will produce anticompetitive effects. Consolidation *per se* is not a competitive evil; only where it results in the exclusion or downplaying of a competing brand by a distributor who would have preferred to distribute or emphasize that competing brand may there be cause for complaint.[12] Although there was some record testimony to the effect that this merger had resulted in the exclusion of a competitor of Franzia from a Mogen David distributor in one instance (I.D. 269), the judge discounted its credibility (I.D. 270), and there was other testimony to indicate that it is unlikely to be a major concern. (I.D. 276 ff.)

On balance we find the record evidence insufficient to sustain a finding that this merger may substantially lessen competition by virtue of any possible adverse effects upon the access of manufacturers to distributional outlets.

The other allegedly anticompetitive effect of the merger to which complaint counsel point to make their case is Coke-New York's effort to reposition Franzia in the [15] marketplace by changing its image: new labels, bottles that "women would be happy to have on their dinner table" (Tr. 883) and, of course, new (and higher) prices. That this effort was met by a chilly market response — dramatically diminished purchases and huge losses for Franzia — is little consolation to complaint counsel. They note that the mere attempt betrays a sinister purpose behind the merger and one that may yet be given effect if the merger challenge is turned back.

The allegation of wrongdoing here is similar to that made in *United Brands, supra,* wherein respondent acquired lettuce-growing land with the intent to market more expensive, brand-differentiated lettuce. While any wine company might on its own, and presumably without legal consequence, attempt to reposition its products,

[12] Alternatively, consolidation may restrain trade by depriving distributors of desired and necessary sources of supply, leading to a decline in the number of distributional outlets. Again, there is little record evidence to indicate that this is a likely effect of the merger.

illegality is premised here, as in *United Brands,* on the fact that the feared effect is threatened as the result of a merger, which bestowed upon Franzia a management disposed to a different philosophy of marketing, and possessed of resources sufficient to give at least limited expression to that philosophy.

Although we cannot agree that the wine industry presents quite the rosy picture of competitive health that respondent suggests[13], we do agree with respondent and Judge Parker that the record presents insufficient basis to conclude that Franzia will, as a result of this merger, be [16] able with impunity to sell old wine in new bottles at a higher price. Were this not so, a more difficult question would be presented, because the practice is plainly not *per se* illegal, and short of entrenchment or attempted monopolization (neither of which seems possible here given Franzia's small size and Coke-New York's limited resources) it is not clear what sort of potential conduct by way of repositioning in the wake of a merger should be grounds for concern. In the circumstances before us, however, this is a question we need not consider.

We find that the record fails to show by a preponderance of the evidence that the instant merger may substantially lessen competition in any line of commerce. Accordingly, an order of dismissal is appended.

Final Order

This matter has been heard by the Commission upon the appeal of complaint counsel from the initial decision and upon briefs and oral argument in support of and in opposition to the appeal. For the reasons stated in the accompanying opinion, the Commission has denied the appeal. Therefore,

It is ordered, That pp. 1–99 of the initial decision of the administrative law judge be adopted as the Findings of Fact of the Commission, except for Finding 65, final two sentences; Findings 210–211; Finding 237; Finding 332; and after changing in Finding 145, line 4, "two" to "one" and deleting "(1) That there are many actual or potential distributors available for wine producers and. . .". In addition, these findings and initial decision pp. 100–112 are not adopted to the extent inconsistent with the accompanying opinion.

It is further ordered, That the complaint be dismissed.

[13] In particular, we agree with complaint counsel that a distinction must be drawn between the ease of entry on a minimal basis at the premium end of the market and entry on a level at which the entrant is capable of affording meaningful competition for the industry leaders catering to the bulk of the market. See *Fruehauf Corp.,* Dkt. 8972, slip op. p.25 (Feb. 22, 1978) [91 F.T.C. at 233], *appeal pending,* No. 78-4053 (2d Cir.) While it may be that anyone with an acre of land, a bathtub, and clean feet can make wine, profitable entry on a scale sufficient to provide meaningful competition for the industry leaders appears to be a considerably more difficult proposition, the dimensions of which are not entirely clear from the record. It is entry of the latter sort with which we must be principally concerned in evaluating the state of competition in an industry.

IN THE MATTER OF

KELLOGG COMPANY, ET AL.

Docket 8883. Interlocutory Order, Jan. 29, 1979

Order denying motion to dismiss the complaint, or in the alternative, to withdraw the proceedings from adjudication and to hold an evidentiary hearing.

ORDER

On November 29, 1978, General Mills filed a motion and supporting memorandum seeking dismissal of the complaint, or alternative relief including withdrawal of the proceedings from adjudication and an evidentiary hearing on the negotiations with Judge Hinkes. Complaint counsel responded on December 12, 1978. The Commission has reviewed these submissions as well as the Order, separate statement of Chairman Pertschuk, and accompanying materials issued on December 8, 1978, and has determined that the relief requested by General Mills should be, and hereby is denied.

I

With respect to General Mills' assertion that the complaint must be dismissed because any continuation of the proceedings will violate General Mills' statutory and constitutional rights, the Commission has concluded that the grounds stated do not warrant the relief requested. In the first place, members of the Commission other than Chairman Pertschuk were unaware of the negotiations with Judge Hinkes at the time that they occurred. Hence, no basis exists in support of a claim that the Commission as a body violated General Mills' rights. Second, Chairman Pertschuk's conduct with respect to the Hinkes contract neither demonstrates a lack of impartiality nor creates an appearance thereof. On the contrary, his conduct was motivated solely by considerations of sound administration and a desire to accomodate the interests of all the parties in bringing these proceedings to an expeditious conclusion. Clearly, the circumstances surrounding his actions would not lead a reasonable person to conclude otherwise.

To the extent that General Mills' motion is based upon contacts between Chairman Pertschuk and Judge Hinkes, it is important to note that Chairman Pertschuk was not acting as an interested party or on behalf of an interested party, but as the "administrative head of the agency." Rules of Practice Section 0.8(a); Reorganization Plan No. 8 of 1950, Section 1(a), 64 Stat. 1264, *reprinted in* 15 U.S.C. 41 App. Further, the Chairman's actions were not related to the merits of the proceeding in any way, nor did he discuss the merits with Judge Hinkes. In light of these facts, the Commission has concluded that there is no actual or apparent lack of impartiality on the part of the Chairman or of any other Commissioner, and that the course of negotiations did not prejudice General Mills' rights in any manner.

II

While General Mills argues that the Commission has an "affirmative duty" to hold an evidentiary hearing, the authorities cited do not warrant such a conclusion. The facts here are clearly distinguishable from the circumstances involved in *United Air Lines, Inc.* v. *CAB,* 281 F.2d 53 (D.C. Cir. 1960), and *Sangamon Valley Television Corp.* v. *United States,* 269 F.2d 221 (D.C. Cir. 1959). Moreover, to the extent that the motion otherwise seeks the information contained in or appended to the Commission's order of December 8, it is dismissed as moot. To the extent that it seeks to probe beyond the explanation already offered, it is denied. General Mills seeks in effect, to probe the predecisional "mental processess" of an agency. Such probing of the mental processes is disfavored, especially where, as here, the reasons for an agency decision are stated. *United States* v. *Morgan,* 313 U.S. 409, 422 (1941); *National Nutritional Foods Ass'n* v. *FDA,* 491 F.2d 1141, 1144–46 (2d Cir.), *cert. denied,* 419 U.S. 874 (1974). In this case, the Chairman has given an ample statement concerning his actions, and related memoranda have been released. See Order of December 8, 1978. Nor has there been any showing of bad faith or improper behavior. On the contrary, the Commission believes that the documents in the record demonstrate the absence of improper behavior or bad faith.

III

Finally, the Commission declines to entertain General Mills' request to withdraw this matter from adjudication and to consider the possibility of settlement. General Mills is entirely free to follow the procedures set forth in Rules of Practice Section 3.25, should it choose to do so.

IV

It is ordered, That (1) General Mills' motion of November 29, 1978, is dismissed as moot to the extent it seeks relief already granted; and

(2) To the extent it seeks relief not previously granted, it is denied in all respects.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

KELLOGG COMPANY, ET AL.

Docket 8883. Interlocutory Order, Jan. 29, 1979

Order denying motion to disqualify FTC Chairman and each other Commissioner advised in advance of proposal to retain ALJ on contract basis.

ORDER

On December 7, 1978, General Foods Corporation filed a motion to disqualify Chairman Pertschuk and each other Commissioner advised in advance of the proposal to retain Judge Hinkes on a contract basis. On January 11, 1979, the Chairman responded to General Foods' motion and refused to disqualify himself. That response was placed on the public docket and served on the parties.

In responding to General Foods' alternative motion that the Commission itself determine whether the Chairman should be disqualified from participating in these proceedings,[1] we see no reason to differ from the result reached by the Chairman. The Chairman's actions were undertaken pursuant to his administrative authority under Reorganization Plan No. 8 of 1950, 64 Stat. 1264. The documents which have been released, and the Chairman's statement of December 8, clearly indicate that his actions in this matter were taken without reference to the merits of the case. Under the circumstances we do not believe that any bias, prejudgment or apparent unfairness has been demonstrated. *Cinderella Career & Finishing Schools, Inc.* v. *FTC*, 425 F.2d 583, 591 (D.C. Cir. 1970); *Amos Treat & Co.* v. *SEC*, 306 F.2d 260, 267 (D.C. Cir. 1962).

As to General Foods' motion to disqualify each of the Commissioners who had advance knowledge of the Hinkes contract, the record is clear that no such Commissioner was so advised. Accordingly,

It is ordered, That the motion of General Foods Corporation to disqualify FTC Chairman Michael Pertschuk and each other Commissioner advised in advance of the proposal to retain Judge Hinkes on a contract basis be, and the same hereby is, denied.

Chairman Pertschuk and Commissioner Pitofsky did not participate.

[1] General Foods argues that the Chairman should be disqualified not only from participating in any decision with respect to the Hinkes contract, but also from participating in any future deliberations in this case.

IN THE MATTER OF

HARPER SALES, INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9070. Complaint, Dec. 19, 1975 — Decision, Feb. 1, 1979

This consent order, among other things, requires a Rush, N.Y. mobile home dealer and its affiliates to cease conditioning the leasing or renting of space in their trailer parks to the purchase of mobile homes and accessories from Harper Sales, Inc. or other designated sources.

Appearances

For the Commission: *Henry R. Whitlock* and *Herbert S. Forsmith.*
For the respondents: *John Stuart Smith, Nixon, Hargrave, Devans & Doyle,* Rochester, N.Y.

COMPLAINT

The Federal Trade Commission, having reason to believe that the parties identified in the caption hereof, and more particularly described and referred to hereinafter as respondents, have violated and are now violating the provisions of Section 5 of the Federal Trade Commission Act, as amended, and it appearing that a proceeding by it in respect thereof would be in the public interest, hereby issues this complaint stating its charges as follows:

I. DEFINITIONS

PARAGRAPH 1. For the purposes of this complaint, the following definitions shall apply:

(a) "Mobile home" means a transportable unit or units designed to be placed without a permanent foundation, connected to utilities, and used or capable of being used for year-round living.

(b) "Mobile home park" means a tract of land utilized specifically for the purpose of renting sites for the placement of mobile homes for residential purposes and in which utility connections and various communal services are commonly provided.

II. RESPONDENTS

PAR. 2. Respondent Harper Sales, Inc. is a corporation organized under the laws of the State of New York with its principal office located at 7500 West Henrietta Road, Rush, New York.

PAR. 3. Respondent Edgewood Park Estates, Inc. is a corporation organized under the laws of the State of New York with its principal place of business located at 4000 Brick Schoolhouse Road, Hamlin, New York.

PAR. 4. Respondent Harper Park-Avon is a partnership organized under the laws of the State of New York with its principal office located at 6150 East Avon–Lima Road, Avon, New York.

PAR. 5. Respondents Ralph R. Harper and John R. Harper are officers of corporate respondent Harper Sales, Inc. They formulate, direct, approve, authorize and control the acts and practices of the corporate respondent including the acts and practices hereinafter set forth. Said individual respondents also are partners in the partnership respondent, Harper Park-Avon. They formulate, direct, approve, authorize and control the acts and practices of the partnership respondent including the acts and practices hereinafter set forth. Their business address is the same as that of corporate respondent Harper Sales, Inc.

PAR. 6. Respondent Harper Sales, Inc. has been, and is now, engaged in the advertising, offering for sale, sale and distribution of mobile homes and mobile home accessories.

In fiscal year 1972, sales of mobile homes by respondent Harper Sales, Inc. were approximately $1,600,000.

PAR. 7. Respondent Edgewood Park Estates, Inc. has been, and is now, engaged in the development and operation of a mobile home park known as Harper Park-Hamlin located at the same address as that of said corporate respondent.

PAR. 8. Respondent Harper Park-Avon has been and is now, engaged in the development and operation of a mobile home park located at 6150 East Avon-Lima Road, Avon, New York.

III. JURISDICTION

PAR. 9. (a) In the course and conduct of its business as aforesaid, respondent Harper Sales, Inc. now causes, and for some time last past has caused, mobile homes and other products to be shipped to purchasers located in states other than New York.

(b) In the course and conduct of its business as aforesaid, respondent Harper Sales, Inc. has purchased and continues to regularly purchase mobile homes and other products from suppliers in states other than New York for the purpose of offering said products for sale, to maintain an available inventory for sale and to fill special purchase orders received from their customers.

(c) In the course and conduct of their business, respondents Edgewood Park Estates, Inc. and Harper Park-Avon have entered into agreements with respondent Harper Sales, Inc. which are essential to make effective the restraints on interstate commerce alleged in Paragraph Eleven hereof.

(d) Respondents maintain, and at all times mentioned herein have maintained, a substantial course of trade in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 10. Except to the extent that competition has been hindered, frustrated, lessened and eliminated by the acts and practices alleged in this complaint, respondents have been and are in substantial competition in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, with persons or firms engaged in the sale of mobile homes and mobile home accessories and with persons or firms engaged in the operation and maintenance of mobile home parks.

IV. VIOLATIONS

PAR. 11. In the course and conduct of their business as aforesaid, respondents have refused to rent sites under the control of Edgewood Park Estates, Inc. and Harper Park-Avon for the accommodation of mobile homes which have not been purchased from Harper Sales, Inc. thereby making the rental of said sites conditional and dependent upon the purchase of mobile homes from Harper Sales, Inc.

V. EFFECTS

PAR. 12. The acts, practices and methods of competition engaged in, followed, pursued or adopted by respondents, as hereinabove alleged, have or tend to have the effect of:

(a) reducing competition in the sale of mobile homes;

(b) foreclosing potential competitors in the sale of mobile homes by raising entry barriers;

(c) foreclosing substantial sales by dealers of mobile homes to actual or prospective tenants of sites in respondents' mobile home parks;

(d) inflating the prices of mobile homes purchased from respondents;

(e) depriving consumers of the benefits of competition.

PAR. 13. The aforesaid acts, practices and methods of competition, constitute unreasonable restraints of trade and unfair methods of competition in or affecting commerce within the intent and meaning of Section 5 of the Federal Trade Commission Act, as amended, and constitute unfair acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Commission having issued its complaint on December 19, 1975, charging that the respondents named in the caption hereof have violated the provisions of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45); and

Respondents and complaint counsel, by joint motion filed December 16, 1976, having moved to have this matter withdrawn from adjudication for the purpose of submitting an executed consent agreement; and

The Commission, by order issued January 11, 1977, having withdrawn this matter from adjudication pursuant to Section 3.25(c) of its Rules; and

Each of the respondents and counsel supporting the complaint having executed an agreement containing a consent order, which includes an admission by the respondents of all the jurisdictional facts set forth in the complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in the complaint, and waivers as required by the Commission's Rules; and

The Commission having considered the matter and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of one hundred and eighty (180) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby makes the following jurisdictional findings and enters the following order:

1. Respondent Harper Sales, Inc. is a corporation organized under the laws of the State of New York, with its principal office located at 7500 West Henrietta Road, Rush, New York.

Respondent Edgewood Park Estates, Inc. is a corporation organized under the laws of the State of New York, with its principal place of business located at 4000 Brick Schoolhouse Road, Hamlin, New York.

Respondent Harper Park-Avon is a partnership organized under the laws of the State of New York with its principal office located at 6150 East Avon-Lima Road, Avon, New York.

Respondents Ralph R. Harper and John R. Harper are officers of corporate respondents Harper Sales, Inc. and Edgewood Park

Estates, Inc. They formulate, direct, approve, authorize and control the acts and practices of Harper Sales, Inc. Said individual respondents are also partners in the partnership respondent, Harper Park-Avon. They formulate, direct, approve, authorize and control the acts and practices of the partnership respondent. Their business address is the same as that of corporate respondent Harper Sales, Inc.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

It is ordered, That Harper Sales, Inc. and Edgewood Park Estates, Inc., corporations, and Harper Park-Avon, a partnership, their successors and assigns, and their officers and partners and Ralph R. Harper and John R. Harper, individually and as officers of said corporations and as partners in said partnership, and respondents' agents, representatives and employees, directly or through any corporation, subsidiary, partnership, division or other device, in connection with the sale of mobile homes or the rental or lease of mobile home sites, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

The offering, execution, maintenance or enforcement of any lease, agreement, understanding or other arrangement which, directly or indirectly, conditions the lease or rental of a mobile home site upon the purchase of a mobile home from a respondent, or a source designated by a respondent. For the purposes of the foregoing sentence a transfer or conveyance of a mobile home site by any respondent to anyone not a respondent which grants any respondent the option or right to purchase such site, shall be deemed to be a lease; and the lease or rental of a mobile home under which the lessor has the option or right to require the lessee to purchase such mobile home as a condition for the continued use of such mobile home, shall be deemed to be a purchase.

Provided, however, that respondents may freely exercise their rights as businessmen, including the right to set reasonable rules, regulations and standards concerning the appearance of mobile homes and acceptance of tenants in respondents' mobile home parks and the operation, maintenance and appearance of mobile homes, mobile home parks and mobile home sites, except insofar as limited by the provisions of this order; and

Provided further, that nothing in this order shall exempt any person or firm from the duty to comply with all applicable laws or regulations which are consistent with the provisions of this order.

It is further ordered, That respondents shall, within thirty (30) days of service of this order, distribute, and obtain a signed receipt therefor, a copy of this order to each of their operating divisions and respondents' employees engaged in the sale or rental of mobile homes or mobile home sites.

It is further ordered, That each individual respondent named herein promptly notify the Commission of the discontinuance of his present business or employment, and of his affiliation with a new business or employment. In addition, for a period of ten years from the effective date of this order, each individual respondent shall promptly notify the Commission of each affiliation with a new business or employment whose activities include the sale of mobile homes or the rental or lease of mobile home sites or of his affiliation with a new business or employment in which his own duties and responsibilities involve the sale of mobile homes or the rental or lease of mobile home sites. Such notice shall include this respondent's new business address and a statement of the nature of the business or employment in which the respondent is newly engaged, as well as a description of respondent's duties and responsibilities in connection with the business or employment.

The expiration of the notice provision of this paragraph shall not affect any other obligation arising under this order.

It is further ordered, That respondents notify the Commission at least thirty (30) days prior to any proposed change in any corporate respondent, or the partnership respondent, such as dissolution, assignment, or sale resulting in the emergence of a successor corporation or partnership, the creation or dissolution of subsidiaries or any other change in the corporation or partnership which may affect compliance obligations arising out of the order.

It is further ordered, That respondents maintain complete business records relative to the manner and form of their continuing compliance with the terms and provisions of this order. Each record shall be retained by respondents for at least three years after it is made.

It is further ordered, That the respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

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IN THE MATTER OF

THE KROGER COMPANY

Docket 9102. Interlocutory Order, Feb. 1, 1979

ORDER AFFIRMING ORDER RULING ON RESPONDENT'S MOTION FOR PRODUCTION OF DOCUMENTS PURSUANT TO § 3.36

Administrative Law Judge Montgomery K. Hyun (the "ALJ") has *sua sponte* certified to the Commission for discretionary review certain of his rulings in connection with respondent's motion for *in camera* production of documents in the files of the Commission. We decline to disturb the ALJ's discovery rulings and, accordingly, we affirm. Our disposition of this matter also moots respondent's application for a stay of further proceedings before the ALJ and for oral argument before the Commission.

The ALJ certified his rulings only because of suggestions by respondent that his continued participation in this matter might be inappropriate in light of the Commission's refusal to grant clearance to one of respondent's attorneys, Mr. Mark Tuller, notwithstanding that both previously served at different times as attorney-advisors to former Chairman Engman.

The standards governing the appearance of former agency employees in Commission proceedings address issues different from those concerning the propriety of participation by administrative law judges. The clearance rules concern impropriety resulting from access to inside information whereas the principal question involving an ALJ's participation is one of bias or prejudgment. Thus, application of these standards may lead to differing results concerning the continued participation of Mr. Tuller and Judge Hyun in this proceeding, notwithstanding that each avers that during his tenure with Chairman Engman he did not participate in any matter pertaining to the respondent.

Here, no question of possible bias of or prejudgment by the ALJ has been raised by the respondent and we can perceive none. Certainly mere access to information in the possession of the Commission casts no shadow on Judge Hyun's ability to render an impartial decision in this matter. Indeed, to suggest otherwise would call into question a judge's ability to review assertedly privileged information *in camera* for the purpose of determining whether the attorney requesting the information is entitled to see it. For these reasons, we find nothing inconsistent about the fact that Mr. Tuller has been denied clearance in this proceeding while Judge Hyun may continue to serve in his altogether different role.

It is ordered, That the ALJ's rulings of January 15, 1979 be, and they hereby are, affirmed; and

It is further ordered, That respondent's motions for a stay and for oral argument, dated January 30, 1979, be, and they hereby are, denied.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

FEDERAL SIGNAL CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2953. Complaint, Feb. 1, 1979 — Decision, Feb. 1, 1979

This consent order, among other things, requires a Chicago, Ill. manufacturer and seller of public safety and communication equipment to cease, in connection with the sale of such products to governmental entities, from exchanging bidding information with its distributors prior to submission of competitive bids, submitting or soliciting the submission of collusive bids, or employing any other business practice that may hinder or prevent competitors from bidding successfully. The firm is also required to cease furnishing governmental bodies seeking to purchase civil defense warning systems with advertisements or specifications that might induce such bodies to limit distribution of invitations to bid; incorporate the name or model number of firm's products into advertisements for bids or specifications; or draft specifications that would restrain, lessen, or prevent the sale of such devices by others.

Appearances

For the Commission: *John T. Hankins* and *David J. Richman.*
For the respondent: *Gary L. Mowder, Schiff, Hardin & Waiter,* Chicago, Ill.

COMPLAINT

The Federal Trade Commission having reason to believe that Federal Signal Corporation has violated the provisions of Section 5 of the Federal Trade Commission Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the interest of the public, hereby issues its complaint, stating its charges as follows:

PARAGRAPH 1. For the purpose of construing this complaint, the following definitions shall apply:

A. "Signal Division products" means any products, or component or accessory thereof, presently or in the future sold by the Signal Division of Federal Signal Corporation, including but not limited to radio equipment, vehicle lights and sirens, speed detecting devices, helmets, visual and audible warning and signaling devices such as lights, sirens, horns and bells, and civil defense warning systems.

B. "Civil defense warning systems" means outdoor warning sirens and components and accessories thereof, which are designed to warn the public of impending enemy attack, storms or other emergency situations. The term includes sirens, activating devices, timers, telephone relays, and other equipment customarily used in connection with the operation of the sirens.

C. "Distributor" shall mean any person, company or other entity purchasing Signal Division products for resale.

D. "Competitive bidding" means the process by which any bid or quotation is made concerning or in response to any solicitation, announcement, advertisement or request by a public body.

E. "Public body" means any unit of federal, state, county or municipal government, or any other organization funded primarily from tax revenues. The term shall include, but not be limited to police departments, fire departments, highway departments and civil defense organizations.

PAR. 2. Federal Signal Corporation, hereinafter referred to as Federal or respondent, is a corporation organized and doing business under the laws of the State of Delaware with its principal office at 120 S. Riverside Plaza, Chicago, Illinois. Federal's sales in 1975 were in excess of $68,000,000.

PAR. 3. Federal, through its Signal Division, is engaged in the manufacture, distribution and sale of public safety and communications equipment for commercial and governmental markets. Federal's sales of Signal Division products were in excess of $29,000,000 in 1975.

PAR. 4. In the course and conduct of its business as aforesaid, respondent causes and has caused its Signal Division products to be shipped from the state in which they are manufactured to distributors and other customers located in other states. Respondent maintains, and at all times mentioned herein has maintained, a substantial course of trade in such products, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 5. Except to the extent that competition has been hindered or restrained by the acts and practices alleged herein, respondent has been and is now in substantial competition, in or affecting commerce, with its own distributors in the offering for sale and sale of Signal Division products and with other manufacturers and distributors in their offering for sale and sale of similar products.

PAR. 6. Federal sells its Signal Division products to distributors located throughout the United States. Federal also sells such products directly to the using customers. Customers of Federal and its distributors include fire departments, police departments, civil defense and disaster warning agencies, and commercial enterprises. In many instances customers purchasing from Federal and its distributors utilize competitive bidding procedures in the purchase of

Signal Division products. In some instances the process of inviting competitive bids is required by law.

PAR. 7. In the course and conduct of its business as aforesaid, respondent, in combination with its distributors, has engaged in the following unfair methods of competition, in or affecting commerce, in connection with the offering for sale, sale and distribution of Signal Division products on a competitive bidding basis:

A) Respondent has exchanged information with its distributors, prior to the submission of bids by respondent and its distributors on particular projects, concerning:

(1) the intent to submit or not to submit a bid;
(2) the prices that will be bid.

B) Respondent has entered into agreements with its distributors, prior to the submission of bids by respondent and its distributors on particular projects, concerning:

(1) whether a bid will be submitted;
(2) which type of equipment will be bid;
(3) what prices will be bid; and
(4) which party will submit the low bid.

C) Respondent has submitted and solicited the submission of collusive bids on particular projects; and

D) Respondent has entered into agreements with its distributors allocating customers among respondent and its distributors.

PAR. 8. The manufacture, distribution and sale of civil defense warning systems constitutes a separate and distinct market. The market for civil defense warning systems is highly concentrated. Federal is the dominant manufacturer in this market and produced more than 70 percent of the civil defense warning systems installed during 1975. Federal has used its dominant position, size and economic power to hinder and frustrate the ability of smaller manufacturers to compete in this market, and to hinder, prevent or lessen competition in the manufacturing and sale of civil defense warning systems. Thus, Federal has been and is now engaged in various monopolistic or other unfair acts, practices, or methods of competition in maintaining a monopoly in the manufacture and sale of civil defense warning systems.

More particularly, Federal has, since at least 1972, adopted and maintained various business practices to restrain, lessen or prevent the sale of civil defense warning systems by others engaged in the manufacture and sale of such products. Respondent has engaged in the following monopolistic acts and practices:

A) Respondent, individually and in combination with its distributors, has participated in the preparation of advertisements soliciting bids and specifications used to obtain and evaluate bids for civil defense warning systems. In the course of this action, respondent has engaged in manipulating the terms contained in such advertisements and specifications with the purpose and effect of hindering or preventing the sellers of other brands of civil defense warning systems from bidding effectively on civil defense warning systems;

B) Respondent has submitted bids, and solicited its distributors to submit bids, which are not intended to secure business, but are intended to hinder or prevent competitors from bidding successfully;

C) In response to requests from public bodies for the names of firms which can bid on civil defense warning systems, respondent generally provides only the names of sellers of its products.

PAR. 9. The aforesaid conduct of respondent in the sale and distribution of Signal Division products, including civil defense warning systems, both individually and in combination with its distributors, has the capacity, tendency, and effect of:

a) restricting, restraining, or eliminating competition among respondent, its distributors, and manufacturers and distributors of competitive products;

b) undermining and subverting the competitive bidding procedures utilized by public bodies and others in the purchase of such products;

c) raising, fixing, stabilizing, and maintaining the prices paid by public bodies for such products;

d) depriving purchasers of such products of the benefits of free and open competition;

e) monopolizing the market for civil defense warning systems;

f) creating, preserving, and increasing barriers to entry into the market for civil defense warning systems.

PAR. 10. The acts and practices of respondent in combination with its distributors, as set out in Paragraph Seven herein, constitute an agreement, combination, or conspiracy to restrict or eliminate competition in the sale and distribution of Signal Division products; are all to the prejudice of actual and potential competitors and buyers of respondent's products, and the public; have a dangerous tendency to and have actually restrained and prevented competition in the sale of Signal Division products and therefore constitute unfair methods of competition, in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act.

PAR. 11. The acts and practices of respondent, as set out in Paragraph Eight herein, both individually and in combination with its distributors, have a tendency to and have actaully restrained and prevented competition in the sale of civil defense warning systems; and have created and maintained in respondent a monopolistic control over the terms and conditions of the sale of such products and therefore constitute unfair methods of competition, in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Denver Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Federal Signal Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 1415 West 22nd St., Oak Brook, Illinois.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

I

It is ordered, That respondent, Federal Signal Corporation, its subsidiaries, successors, assigns, officers and directors, and respondent's agents, representatives and employees, individually or in concert with others, directly or indirectly, or through any corporate or other device, in connection with the distribution, offering for sale, or sale of Signal Division products by Federal or any of its distributors, to public bodies on a competitive bidding basis, in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, shall forthwith cease and desist from:

1. Exchanging information with any of its distributors, prior to any bid being submitted on any particular project, concerning:

a) the intent to submit or not to submit a bid; or
b) the price(s) that will be bid;

2. Entering into any agreement or understanding with any of its distributors, prior to any bid being submitted on any particular project, concerning:

a) the intent to submit or not to submit a bid;
b) the type of equipment that will be bid;
c) the price(s) that will be bid; or
d) the party which will submit the low bid;

3. Submitting or soliciting the submission of any collusive bid;
4. Allocating or attempting to allocate customers among respondent and its distributors, provided that respondent may furnish the name of one or more of its distributors to any buyer or prospective buyer of respondent's products.

II

It is further ordered, That respondent, in connection with the distribution, offering for sale, or sale of civil defense warning systems by Federal or any of its distributors, to public bodies on a competitive bidding basis, in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, shall forthwith cease and desist from:

1. Furnishing, directly or indirectly, prior to the submission of any written bid, any written specification to such public body (other than specifications established by any department of the federal government) to be substantially incorporated into materials used to obtain or evaluate bids;

2. Influencing or attempting to influence any such public body to:

a) limit the distribution of invitations to bid to respondent and/or its distributors;

b) incorporate the name or model number of any of respondent's products into advertisements for bids or specifications used to obtain or evaluate bids;

c) draft specifications which disqualify sellers of competitive products from bidding effectively;

3. Preparing any part of any advertisement for bids or specification used by a public body to obtain or evaluate bids.

Nothing contained in Part II of the order shall prohibit respondent from conducting surveys of civil defense warning system needs for public bodies and providing quotations containing descriptions of civil defense warning systems and estimated costs. All such quotations shall contain the following statement in close proximity to the product description:

> Civil defense warning systems produced by other manufacturers may provide adequate coverage for the area surveyed even though such systems may contain differing numbers of sirens having different decibel ratings or functioning in a different manner. The names and addresses of other recognized manufacturers of civil defense warning systems will be provided upon request.

It is further ordered, That respondent, upon request by a public body, provide the names and addresses of all other manufacturers of civil defense warning systems known to respondent.

III

It is further ordered, That respondent, for a period of five years from the date of service of this order:

1. Institute a continuing surveillance program to insure that its distributors of civil defense warning systems are not engaging in any act or practice which, if engaged in by respondent, would violate Paragraphs 1, 2, or 3 of Part II of this order;

2. Upon receiving information indicating that any of its distributors of civil defense warning systems has engaged in any such act or practice, respondent shall obtain the written assurance of such

distributor that such conduct shall not again occur. If the distributor fails to provide such written assurance, respondent shall forthwith cease and desist from supplying civil defense warning systems to such distributor;

3. Upon ascertaining that a distributor, after having given such written assurance, has again engaged in any such act or practice, forthwith cease and desist from supplying civil defense warning systems to such distributor.

IV

It is further ordered, That respondent, for a period of three years from the date of service of this order, in connection with each bid on civil defense warning systems submitted to a public body:

1) include a copy of the letter set forth in Appendix A hereto and a copy of this order with each such bid; and

2) maintain a file concerning each such bid, such file to include a copy of the bid and accompanying letter, all work papers used in computing the bid, and a copy of each document furnished to the public body involved.

The files described herein shall be made available for Commission inspection upon reasonable notice.

V

It is further ordered, That respondent shall within thirty days after service upon it of this order, distribute a copy of the order to each of the respondent's operating divisions, to each of its present corporate officers and to each domestic sales representative in the Signal Division, and to its future corporate officers and Signal Division domestic sales representatives within five days of their assumption of office or employment with respondent corporation.

VI

It is further ordered, That respondent shall notify the Commission at least thirty days prior to any proposed change in its organization, such as dissolution, assignment or sale resulting in organization, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of this order.

It is further ordered, That the respondent shall within sixty days after service upon it of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

APPENDIX A

(Official Stationery of Federal Signal Corporation)

Dear ________________:

Federal Signal Corporation has entered into a consent agreement with the Federal Trade Commission concerning the company's competitive bidding practices. The agreement is for settlement purposes only and does not constitute an admission of any law violations. Part I of the Order issued pursuant to the agreement applies to the sale of all Signal Division products. Parts II, III, and IV apply to sales of civil defense warning systems.

A copy of the order issued by the Commission is enclosed. If, in connection with this bid or at any time in the future, you believe that Federal has engaged in any of the practices prohibited by the Order, report the details in writing to:

Federal Trade Commission
Washington, D. C. 20580

You are also requested, at your option, to send a copy of any such letter to:
Federal Signal Corporation
Attention: President

Very truly yours,

(Name)
President
Federal Signal Corporation

IN THE MATTER OF

INDIANA FEDERATION OF DENTISTS

Docket 9118. Interlocutory Order, Feb. 5, 1979

ORDER DENYING PETITION OF STATE OF INDIANA TO INTERVENE

The State of Indiana, by its Attorney General, has appealed from a decision of Administrative Law Judge Paul R. Teetor (the "ALJ") denying its application to intervene in this proceeding. Because we do not believe that there has been a sufficient showing of the necessity for intervention, we cannot grant the petition.[1] The State of Indiana, however, is granted leave to appear in the proceeding as *amicus curiae* and to submit such briefs as it deems necessary to adequately represent the interests of the State on its own behalf and as *parens patriae* for its citizens.

The complaint in this matter was issued in October, 1978, and charges the respondent Indiana Federation of Dentists with, *inter alia,* illegally conspiring to frustrate cost control programs administered by a number of insurance companies. In essence, the respondent and its members, a small group of Indiana dentists, are alleged to have agreed among themselves to refuse to submit X-rays and other diagnostic tests to insurers, who seek such information in order to assure that a dentist's proposed treatment is the least expensive treatment adequate to remedy a patient's dental ills.

Respondent has raised as an affirmative defense the assertion that its members are proscribed by Indiana law from submitting diagnostic materials, such as X-rays, to third party insurance payers, because such companies may employ non-dentists to review the X-rays. Respondent notes that Indiana law forbids the practice of dentistry by non-dentists, and contends that review of X-rays constitutes the practice of dentistry. Under this so-called "state action" defense, respondent in effect asserts that it is acting as a private attorney general to enforce Indiana law.

The State of Indiana apparently agrees with respondent about what constitutes the "practice of dentistry,"[2] and seeks permission

[1] Unlike the ALJ, we do not believe that the proposed intervenor's status as a state bars its application here. Section 5(b) of the Federal Trade Commission Act provides: "Any person, partnership, or corporation may make application, and upon good cause shown may be allowed by the Commission to intervene and appear in said proceeding by counsel or in person." The term "person" as used in the antitrust laws may emcompass a state, *Lafayette* v. *Louisiana Power & Light Co.,* 435 U.S. 389 (1978). A consistent interpretation should be given to the implementing provision of the Commission's Rules of Practice, Section 3.14, albeit slightly different phraseology is used there. Indeed, the Commission has previously permitted intervention by sovereign states, *see e.g., Florida Citrus Mutual,* Dkt. 6074 (February 12, 1953).

[2] *See* Unofficial Advisory Letter, dated March 14, 1974, from Curtis Plopper, Deputy Attorney General of the

(Continued)

to intervene both to press this point and, as *parens patriae,* to protect its citizens from the unauthorized practice of dentistry in Indiana. While we appreciate the State's concerns, we are not convinced that Indiana must be made a party to this proceeding in order for that State to present effectively its views on the proper interpretation of Indiana law. No witnesses need be examined, nor any documentary evidence introduced, to establish Indiana's point of statutory construction, and as the State itself recognizes in its Memorandum in Support of Application for Review (p. 4), "*amicus curiae* . . . is the traditional role accorded to those concerned with the precedential impact of adjudicative decisions." Where, as here, Indiana's arguments are wholly legal in nature and will relate more to such concerns as legislative history than to respondent's challenged practices, *amicus curiae* status should satisfactorily protect the State's interest.

Even assuming *arguendo* that some evidentiary inquiry or undertaking is necessary to properly present the "state action" defense, the State of Indiana has advanced no reason why that defense cannot adequately be presented by counsel for respondent. Were the State intending to raise different or even supplemental concerns, our response might be otherwise, but the Deputy Attorney General candidly concedes that "[t]he State does not contemplate raising issues distinct from those raised in the Complaint and the Answer." Memorandum in Support of Application for Review, p. 8. As we said in *Firestone Tire and Rubber Co.,* 77 F.T.C. 1666, 1668 (1970), persons seeking intervention must raise substantial issues "which would not otherwise be properly raised or argued." Given the apparent identity of interest between respondent and the State, and given that the State has not even contended that respondent will not adequately present the "state action" defense, we cannot say that the *Firestone* test has been met.

We are sympathetic to the concerns raised by the State and appreciate its interest in assisting the Commission in reaching a just result in this adjudicative proceeding. We hope that the State will avail itself of the opportunity to file *amicus* briefs as the need arises, so that both the ALJ and the Commission can have the benefit of its views on the proper application of Indiana law to the facts at bar.

It is ordered, That the application for intervention filed by the State of Indiana be, and it hereby is, denied.

State of Indiana, to Dr. Raymond Rothaar, President, Indiana Board of Dental Examiners, in which the author apparently concludes that review of dental X-rays constitutes the "practice of dentistry" under Indiana law. The letter concludes by stating that "[t]he views expressed herein are those of the writer and are not to be considered to be the opinion of the Attorney General of Indiana, nor a precedent of the Attorney General's office."

IN THE MATTER OF

RHINECHEM CORPORATION, ET AL.

Docket 9116. Interlocutory Order, Feb. 12, 1979

ORDER DENYING RESPONDENTS' MOTION FOR DISMISSAL OF COMPLAINT

Administrative Law Judge Ernest G. Barnes has certified to the Commission, without recommendation, a motion by two respondents, Allegheny Ludlum Industries, Inc. ("ALI"), and Chemetron Corporation, to dismiss the complaint. We deny the motion, believing that the public interest would be better served by allowing this case to proceed.

Respondents' ground for dismissal is that the proposed acquisition by Rhinechem Corporation of the Pigments Division of Chemetron, a subsidiary of ALI, has been terminated. This acquisition, however, was not abandoned until after a United States District Court, upon motion of the Commission, issued an injunction against respondents barring the acquisition during the pendency of a Commission administrative proceeding and any subsequent judicial review. In granting the injunction, the court found that the Commission, which had contended that the acquisition would violate Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act, had demonstrated a sufficient likelihood of ultimate success on the merits.

It is conceded, and the Commission has so held, *see, e.g., British Oxygen Co., Ltd.,* 86 F.T.C. 1241, 1334-35 (1975), *rev'd on other grounds,* 557 F.2d 24 (2d Cir.1977), that the prohibitions of Section 7 of the Clayton Act are directed against the acquiring company, rather than the company to be acquired. Nevertheless, it is also clear that the moving respondents may be properly charged with a violation of Section 5 of the Federal Trade Commission Act for entering into a merger agreement which, complaint counsel contend, violates Section 7 of the Clayton Act. *Dean Foods Co.,* 70 F.T.C. 1146, 1288-92 (1966); *British Oxygen Co., Ltd., supra* at 1334. *Cf. Grand Union* v. *FTC,* 300 F.2d 92 (2d Cir. 1962). Thus, even though the Commission has withdrawn this matter from adjudication with respect to Rhinechem Corporation in order to consider a proferred consent agreement, the complaint nonetheless states a cause of action under Section 5 of the Federal Trade Commission Act against the moving respondents. In Section 5 cases, it is well established that the discontinuance or abandonment of a practice, especially where not entirely voluntary, does not preclude the issuance of an appropriate cease and desist order. *E.g., Coro, Inc.* v. *FTC,* 338 F.2d 149 (1st Cir. 1964), *cert. denied,* 380 U.S. 954 (1965). Accordingly,

It is ordered, That respondents' motion for dismissal of the complaint, dated December 19, 1978, be, and it hereby is, denied.

In the Matter of

KAUFMAN AND BROAD, INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2954. Complaint, Feb. 12, 1979 — Decision, Feb. 12, 1979

This consent order, among other things, requires a Los Angeles, Calif. builder and seller of residential housing to cease misrepresentations of fact and using any other unfair or deceptive practices in the advertising, sale and construction of consumer housing. The firm is also required to furnish prospective customers with disclosures regarding construction materials and components; as well as information relating to the land, taxes and community facilities. Further, the company is required to provide home purchasers with warrantees patterned on the housing industry's Home Owners Warranty program; and to employ the industry's standards in home construction and repair. Additionally, provisions in the order entitle original owners of company homes purchased from January 1, 1972, to have specified defects repaired, and requires the firm to repurchase the homes at the original price, should it fail to make proper repairs in a timely manner. The order also provides that disputes concerning repairs may be settled through third-party arbitration.

Appearances

For the Commission: *Blanche Stein, Richard A. Palewicz* and *Jerome S. Lamet.*

For the respondents: *Elroy Wolff, Sidley & Austin,* Washington, D.C.

Complaint

The Federal Trade Commission, having reason to believe that respondents Kaufman and Broad, Inc., a corporation, Kaufman and Broad Homes, Inc., a corporation, and Kaufman and Broad Home Sales, Inc., a corporation, have violated Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), and believing that a proceeding by it in respect thereof is in the public interest, hereby issues its complaint as follows:

I

For purposes of this complaint, "on-site residential housing" shall mean housing structures, including lots, consisting of single family dwelling units or housing structures consisting of multi-family dwelling units (including condominiums) represented and sold by respondents as completely constructed or partially constructed units.

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II

PARAGRAPH 1. Respondent Kaufman and Broad, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Maryland with its principal place of business located at 10801 National Boulevard, Los Angeles, California.

Respondent Kaufman and Broad, Inc. has numerous subsidiaries in various States of the United States.

Respondent Kaufman and Broad, Inc. uses the trade styles: Kaufman & Broad, Kaufman and Broad, and Kaufman and Broad homes in the course and conduct of its business.

Respondent Kaufman and Broad Homes, Inc. is a wholly-owned subsidiary of respondent Kaufman and Broad, Inc., and is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois with its principal office and place of business located at 900 Jorie Boulevard, Oak Brook, Illinois.

Respondent Kaufman and Broad Home Sales, Inc. is a wholly-owned subsidiary of respondent Kaufman and Broad Homes, Inc., an Illinois corporation, and is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois with its principal office and place of business located at 900 Jorie Boulevard, Oak Brook, Illinois.

PAR. 2. Respondents are now and for some time last past have been engaged in the production, advertising, offering for sale or sale of on-site residential housing to the public. Gross sales of on-site residential housing by respondent and its subsidiaries in 1973 was approximately $306,763,000, in 1974 approximately $256,567,000, in 1975 approximately $250,482,000, and in 1976 approximately $283,183,000.

III

PAR. 3. In the course and conduct of its business, as aforesaid, respondent Kaufman and Broad, Inc. has formulated and established uniform and standardized methods, practices and procedures for the regulation, supervision and monitoring by respondent of the bookkeeping, accounting, financial, purchasing, sales, personnel, customer relations and management operations of its subsidiaries located in various States of the United States.

In the course and conduct of its business, as aforesaid, respondent Kaufman and Broad Homes, Inc., an Illinois corporation, has caused to be published in newspapers of interstate circulation advertisements which are designed and intended to induce the public to purchase respondent's on-site residential housing.

In the course and conduct of its business, as aforesaid, respondent

Kaufman and Broad Homes Sales, Inc., an Illinois corporation, has entered into contracts for the purchase of respondent's on-site residential housing with members of the public residing outside the State of Illinois.

Therefore, each of the corporate respondents is engaged in or affects "commerce," as "commerce" is defined in the Federal Trade Commission Act and has been continuously so engaged for several years.

IV

PAR. 4. In the course and conduct of their business, as aforesaid, and for the purpose of inducing the public to purchase respondents' on-site residential housing, respondents have made statements and representations in advertising brochures and in advertising inserted in newspapers of interstate circulation.

Typical and illustrative of such statements and advertising representations, but not all inclusive thereof, are the following:

We're America's largest publicly held company whose primary business is on-site housing. We know the housing business!

* * * * * * *

Because Kaufman and Broad is Chicago's largest home builder, we can build fine homes. . .our size enables us to use good workmen, quality materials and money-saving tools and techniques.

* * * * * * *

Ask your Kaufman and Broad salesman about our exclusive Buy Back Plan. It is an extra assurance to you made possible by Kaufman and Broad's full confidence in the value and quality construction of the homes they build. After one year, if you are not completely satisfied with your home, Kaufman and Broad will give you your money back. . .

* * * * * * *

Because of our size, we are able to give you a bigger better home for your money. . .

* * * * * * *

You can have confidence in Kaufman and Broad. Most homeowners do.

* * * * * * *

Kaufman and Broad's years of experience also insure sound planning and design in all community developments. The added value of this experience will be appreciated by the home owner in his day-to-day living as he realizes the thought and care that has gone into the development of his home and community.

* * * * * * *

Kaufman & Broad provides a kind of quality control that only can be offered because of its huge size.

* * * * * * *

. . .the best locations–there are Kaufman and Broad communities in many of the most popular Chicago suburbs. Because we're first, we get first choice of all the prime land that's available.

* * * * * * *

Immediate occupancy No closing costs

* * * * * * *

F.H.A. loans available. . .

* * * * * * *

. . .Homes with garages, basements, family rooms, patio kitchens, glamour vanity baths and much more - all the room your family needs

* * * * * * *

. . .with a garage and basement,. . .

* * * * * * *

3 & 4 bedroom homes from $20,990.

* * * * * * *

. . .2, 3 and 4 bedroom homes from $19,990 . . . These low prices available for a limited time only.

* * * * * * *

You needn't stray far from your home in Appletree to reach all the things you need.

1. Rich Central High
2. Marion High (Parochial)
3. Southwood Jr. High
4. Willowview Elementary
5. Baker Avenue Kindergarten
6. Loretto Lane Kindergarten
7. St. Emeric's Elementary (Parochial)
8. St. John Lutheran School
9. Hillcrest High

PAR. 5. By and through the use of the above–quoted statements and representations and others of similar import and meaning not expressly set out herein, respondents have represented, and are now representing, directly or by implication that:

1. Housing sold by respondents is built in accordance with good construction practices in the housing industry.

2. Housing sold by respondents is of top quality workmanship.

3. Housing sold by respondents is constructed in accordance with the Minimum Property Standards for such housing as required by the U.S. Department of Housing and Urban Development.

4. Housing sold by respondents is constructed in accordance with plans and specifications approved by the U.S. Department of Housing and Urban Development.

5. By and through the use of the words "quality materials," "quality construction," "quality control," and other words of similar import and meaning not specifically set out herein, respondents' housing is free from structural or other defects that could impair such housing for ordinary use as homes or habitations.

6. Respondents have a unique quality control program that provides for the inspection of their housing at various stages in construction to insure that such housing is of quality workmanship and is free from structural and other defects.

7. By and through the use of the words "best locations" and "first choice of all the prime land that's available," and other words of similar import and meaning not specifically set out herein, land used by respondents for building sites is not subject to any severe limitations that may affect the use of such land for the construction of on-site residential housing sold by respondents.

8. Respondents' advertised homes are available for immediate occupancy.

9. All homes offered for sale by respondents include a family room and a garage or a basement and a garage in the advertised price.

10. All rooms advertised as bedrooms in respondents' 4-bedroom homes are suitable for sleeping purposes.

11. Respondents' advertised prices for homes are for a limited time only.

12. Respondents' housing is sold to purchasers free of all closing costs.

13. Schools listed in respondents' advertising are in school districts where respondents' housing is located.

PAR. 6. In truth and in fact:

1. All housing sold by respondents was not built in accordance with good construction practices in the housing industry. In some houses, fire walls were improperly anchored, foundation walls were not covered with membrane waterproofing to prevent water seepage

into habitable spaces, or weep holes were absent in brick veneer walls for the escape of water.

2. All housing sold by respondents was not top quality in workmanship. In some houses, siding was not properly anchored, roof sheathing did not meet with roof edges, spaces between foundation walls and sill plates were not sealed to prevent the entry of air and moisture, or piping and bathroom fixtures were not properly installed.

3. All housing sold by respondents was not constructed in accordance with the Minimum Property Standards for such housing as required by the U.S. Department of Housing and Urban Development. In some houses, front stoops were improperly supported and/or anchored to foundation walls, sill plates were not properly matched to foundation walls to prevent seepage of water and/or air into the interior of the house, or paint used on kitchen and bathroom walls was not washable as required by such standards.

4. All housing sold by respondents was not constructed in accordance with the plans and specifications approved by the Department of Housing and Urban Development. In some houses, there were deviations and omissions from such plans and specifications that affected the quality of a component part in the house.

5. All housing sold by respondents was not free from structural or other defects that could impair such housing for ordinary use as homes or habitations. In some houses, walls were not properly supported by foundations, floor girders were not properly supported to prevent sagging floors, or foundations contained cracks due to structural failures.

6. Respondents did not have a unique quality control program that provides for the inspection of their housing at various stages in construction to insure that such housing is of quality workmanship and is free from structural and other defects. In many cases, housing constructed and delivered by respondents to purchasers has been characterized by defects that could have been avoided through proper inspections by supervisory personnel.

7. All land used by respondents for building sites was not free from severe limitations that may affect the use of such land for the construction of on-site residential housing sold by respondents. In some cases, such land was subject to frequent or continuous water saturation, slow run-off of surface water, ponding of water in various places or poor drainage that could result in frost-heave and shrink-swell.

8. Homes advertised by respondents as available for "immediate occupancy" were in many cases unavailable for occupancy by

purchasers until many months after the purchase agreement had been signed.

9. Homes advertised by respondents as including a family room and a garage or a basement and a garage did not in many cases include such features in the advertised price. Such features were optional rather than standard and available only upon the payment of an additional charge. In some cases, certain optional features were unavailable even for the payment of an additional charge.

10. All rooms advertised as bedrooms in respondents' 4-bedroom homes were not suitable for sleeping purposes. Rooms represented as bedrooms were unsuitable for such use because they were constructed with insufficient insulation, inadequate waterproofing or other construction defects.

11. Sales prices of homes advertised as being for "a limited time only" were offered by respondents over a substantial period of time.

12. Respondents' housing was not sold to purchasers free of all closing costs. In many cases, charges and fees incident to the sale of respondents' housing were actually imposed upon purchasers.

13. Schools represented as being located in certain school districts were not located in such school districts and were, therefore, unavailable to the purchasers of respondents' homes located in such school districts.

Therefore, the statements and representations as set forth in Paragraph Five above were false, misleading and deceptive.

V

PAR. 7. In the course and conduct of their business, as aforesaid, and for the purpose of inducing the public to purchase respondents' on-site residential housing, respondents have made oral representations through their sales representatives and agents concerning the residential housing which respondents offer for sale.

Among the oral statements and representations made, but neither verbatim nor all-inclusive thereof, are the following:

1. That parks, playgrounds or schools will be built or developed in the near future in certain communities where respondents' residential housing is located.

2. That public transportation facilities will be available within certain communities where respondents' residential housing is located.

3. That landscaping in certain of respondents' housing developments would include four inches of topsoil in each purchaser's lot that would be suitable to support plant growth.

4. That the tax credit furnished at "closing" by respondents to certain purchasers of their on-site residential housing represented the estimated assessed valuation of the property for tax purposes.

PAR. 8. In truth and in fact:

1. No park, playground or school has been built or developed in certain designated communities, and have not been anticipated or authorized for such building and development in the near future, as represented by respondents to purchasers and prospective purchasers of respondents' residential housing.

2. No public transportation facilities have been made available within certain designated communities, and have not been anticipated or authorized for such availability in the near future, as represented by respondents, to purchasers and prospective purchasers of respondents' residential housing.

3. Landscaping in certain of respondents' housing developments where four inches of topsoil was to be included did not include four inches suitable for plant growth. The soil furnished was clay or a mixture of clay with gravel or debris.

4. The tax credit furnished at "closing" by respondents to certain purchasers of their on-site residential housing did not represent the actual assessed valuation of the property for tax purposes. At the time such tax credit was furnished by respondents, respondents knew or should have known that the actual assessed valuation of the property was significantly higher.

Therefore, the statements and representations as set forth in Paragraph Seven above were and are false, misleading and deceptive.

VI

PAR. 9. In the course and conduct of their business, as aforesaid, and for the purpose of inducing the public to purchase respondents' on-site residential housing, respondents have made representations through model home samples and other devices concerning certain features in connection with the sale and delivery of such housing.

Illustrative of such model home representations, but not all inclusive thereof, are the following:

1. That a kitchen displayed in respondents' one-story model ranch home, Style R-24, would be identical to that delivered to purchasers of that particular style house.

2. That an open staircase with wrought iron railing displayed in respondents' Style S-2 McIntosh model home would be identical to that delivered to purchasers of that style house.

3. That mattresses displayed in bedrooms of certain of respondents' model homes were 74-1/2 inches in length.

PAR. 10. In truth and in fact:

1. Kitchens delivered to many purchasers of respondents' one-story ranch house, Style R-24, included a walled-off storage area that was not present in the model home displayed to purchasers and which had the effect of reducing the size of the kitchen by approximately four feet by eight feet.

2. An open staircase was not delivered to many purchasers of respondents' Style S-2 McIntosh house. Instead, such purchasers received a walled-in staircase.

3. Mattresses and beds used as display in bedrooms of certain of respondents' model homes were less than 74-1/2 inches in length thereby causing said rooms to appear larger than their actual dimensions.

Therefore, the representations as set forth in Paragraph Nine above were and are false, misleading and deceptive.

VII

PAR. 11. In the course and conduct of their business, as aforesaid, and for the purpose of inducing the public to purchase respondents' on-site residential housing, respondents have included written statements in their advertising brochures, sales documents, and advertising inserted in newspapers of interstate circulation and in oral representations made by their sales representatives and agents concerning warranties against defects in housing that respondents offer for sale.

Typical and illustrative of said statements and representations are the following:

Satisfaction Guaranteed by Kaufman and Broad

In addition to an unprecedented five-year new home warranty Kaufman and Broad provides 24-hour customer service

* * * * * * *

Kaufman and Broad explains why you should buy a home NOW. . .exclusive 5-year structural warranty. . .

* * * * * * *

. . .every house built by Kaufman and Broad carries our exclusive New Home Structural Warranty. This unique assurance of quality, unheard of in the entire building industry, guarantees the lasting value of a Kaufman and Broad Home.

* * * * * * *

The Home. . .has been constructed with the greatest care and workmanship. . .in substantial conformity with the plans and specifications on file in its office.

Should any major structural defect exist which, at any time within five (5) years from the date hereof, would directly result in the loss or impairment of such Home as a single family residence, Kaufman and Broad Homes, Inc. hereby binds itself to remedy such defect at no cost or obligation to such Purchaser; provided that notice of such defect is delivered to Kaufman and Broad Homes, Inc. . . .

* * * * * * *

Everything guaranteed for one year

* * * * * * *

Covers everything

* * * * * * *

Anything wrong would be repaired or replaced

PAR. 12. By and through the use of the statements and representations quoted in Paragraph Eleven hereinabove, and others of similar import and meaning not expressly set out therein, respondents represent and imply and have represented and implied:

1. That respondents' five-year warranty represents an unqualified obligation on the part of respondents to remedy all structural defects in their on-site residential housing of the kind that would result in the loss or impairment of such housing as a residence.
2. That under their five-year warranty respondents will remedy any structural defects provided that proper notice is given to respondents.
3. That respondents will repair all structural defects in on-site residential housing sold under their five-year warranty.
4. That all of respondents' on-site housing sold under five-year warranties is in substantial conformity with respondents' plans and specifications for such housing.
5. That the one-year warranty offered by respondents in connection with their on-site residential housing is an unqualified obligation on the part of respondents to repair any and all defects and to repair or replace any and all defective materials used in construction arising within one year from date of conveyance of such housing by respondents to the purchaser.
6. That purchasers of respondents' on-site residential housing who invoke respondents' one-year warranty may reasonably expect that respondents will repair any and all defects and will repair or replace any and all defective materials used in construction.

PAR. 13. In truth and in fact:

1. The five-year warranty was not an unqualified obligation on the part of respondents to remedy structural defects in the on-site residential housing sold by respondents.

2. In many cases even after proper notice was given to respondents of structural defects under the five-year warranty, respondents neglected, refused, or ignored making repairs under the warranty.

3. Respondents did not, in all cases, repair structural defects in on-site residential housing sold under their five-year warranty.

4. Not all on-site residential housing sold by respondents under their five-year warranty was in substantial conformity with respondents' plans and specifications for such housing.

5. The one-year warranty offered by respondents in connection with their on-site residential housing did not represent an unqualified obligation on the part of respondents to repair any and all defects and to repair or replace any and all defective materials used in construction arising within one year from the conveyance of such housing to the purchaser.

6. When purchasers of respondents on-site residential housing invoked respondents' one-year warranty, respondents did not, in all cases, repair any and all defects or repair or replace any and all defective materials used in construction. When requests for repairs or replacements were made by purchasers under such warranties, respondents, in many cases, failed to make such requested repairs or replacements.

Therefore, the statements and representations as set forth in Paragraphs Eleven and Twelve above were and are false, misleading and deceptive.

VIII

PAR. 14. In the course and conduct of their business, as aforesaid, and for the purpose of inducing the public to purchase respondents' on-site residential housing, respondents made statements and representations in advertising brochures and in advertising inserted into newspapers of interstate circulation concerning warranties and guarantees.

In connection with such advertised warranties and guarantees, respondents failed to adequately disclose material terms and conditions of such warranties and guarantees such as (1) the nature and extent of such warranties and guarantees, (2) the conditions and limitations of such warranties and guarantees, and (3) the manner in which respondents will perform under such warranties and guarantees.

Thus, respondents failed to disclose such material facts concerning warranties and guarantees which, if known to certain prospective purchasers, would be likely to affect their consideration of whether or not to purchase respondents' on-site residential housing.

Therefore, respondents' failure to disclose such material facts was unfair, false, misleading or deceptive acts or practices.

PAR. 15. In the ordinary course of their business, as aforesaid, respondents caused members of the public seeking to purchase homes from respondents to enter into written sales contracts with respondents which contracts contain a provision reserving to respondents the right to designate the mortgagee.

By and through the use of said written provisions contained in respondents' sales contracts as aforesaid, respondents have precluded purchasers from the opportunity of comparing various alternative credit terms that may be available to such purchasers on more favorable terms from other sources.

Therefore, the acts and practices as set forth above hereof were unfair, false, misleading or deceptive.

PAR. 16. In the course and conduct of their aforesaid business and at all times mentioned herein, respondents have been and are now in substantial competition, in or affecting commerce, with corporations, firms and individuals in the construction and sale of on-site residential housing.

PAR. 17. The use by respondents of the aforesaid unfair, misleading and deceptive statements, representations and practices has had the capacity and tendency to mislead members of the purchasing public into the purchase of substantial numbers of respondents' on-site residential housing.

PAR. 18. The aforesaid acts and practices of the respondents as herein alleged were all to the prejudice and injury of the public and of respondents' competitors and constituted and now constitute unfair methods of competition and unfair and deceptive acts and practices, in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Chicago Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and the complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Kaufman and Broad, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Maryland, with its principal office and place of business located at 10801 National Boulevard, Los Angeles, California.

Respondent Kaufman and Broad Homes, Inc. is a wholly-owned subsidiary of respondent Kaufman and Broad, Inc. and is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois with its principal office and place of business located at 900 Jorie Boulevard, Oak Brook, Illinois.

Respondent Kaufman and Broad Home Sales, Inc. is a wholly-owned subsidiary of respondent Kaufman and Broad Homes, Inc., and is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois with its principal office and place of business located at 900 Jorie Boulevard, Oak Brook, Illinois.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

Order

I

Definitions

"On-site residential housing" shall mean housing structures, including lots, consisting of single family dwelling units or housing structures, consisting of multi-family dwelling units (including condominiums) represented and sold by respondents in the United States as completely constructed or partially constructed units.

An "express warranty" as used in this order shall mean any written affirmation of fact or written promise made or assigned by respondents to a purchaser as part of the transaction of the sale of a unit of on-site residential housing.

The "HOW warranty" as used in this order shall mean the warranty issued under the Home Owners Warranty Corporation's national home warranty program.

A "major construction defect" as used in this order shall mean a "major construction defect" as defined in the Home Owners Warranty Corporation Home Warranty Agreement attached hereto as Appendix A.

The term "approved standards" as used in this order shall mean "approved standards" as defined in the Home Owners Warranty Corporation Home Warranty Agreement attached hereto as Appendix A.

A "legal holiday" as used in this order shall mean any one of the following business holidays: New Year's Day, Washington's Birthday, Memorial Day, Independence Day, Labor Day, Veteran's Day, Thanksgiving Day, Christmas Day.

"Closing costs" as used in this order shall mean all the charges and fees imposed directly or indirectly upon a purchaser incident to the sale of real property. Specifically excluded herefrom are escrow deposits and impounds.

"Past purchaser" as used in this order shall mean "past purchaser" as that term is defined in Part VII and Part VIII of this order.

"Repurchase price" as used in this order shall mean the price at which the home was purchased by the original purchaser from respondents or from any of respondents' subsidiaries.

"Receipt" as used in this order in connection with the receipt by respondents of written requests for repairs from purchasers and past purchasers of respondents' housing shall mean three (3) days following the date post-marked on any letter sent through the United States mail; *provided,* that the actual date of receipt of any written request may be established by other means regardless of the method of delivery that was, in fact, used.

II

It is ordered, That respondents Kaufman and Broad, Inc., a corporation, Kaufman and Broad Homes, Inc., a corporation, and

Kaufman and Broad Home Sales, Inc., a corporation, their successors and assigns, and their officers, and respondents' agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with the conduct and operation of their business in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act in the production, advertising, offering for sale or sale of a unit of on-site residential housing, do cease and desist from:

1. Selling and delivering any housing unit for use as on-site residential housing which is not built in accordance with the approved standards or which contains a major construction defect without taking the necessary action to repair, replace, or to pay the cost of repairing or replacing the defect in such housing unit in accordance with the provisions of respondents' express warranty required under Part III B of this order.

2. Failing, in connection with the express warranty required under Part III B of this order to:

(a) Make repairs in a workmanlike manner to a unit of on site residential housing where such repairs are required under respondents' warranty.

(b) Make repairs with materials or components identical to, or of an equal or better grade or quality than, the materials or components used in the original construction of the particular unit of on-site residential housing where such repairs are required under respondents' warranty.

3. Failing to adhere to Minimum Property Standards for the construction of on-site residential housing as required by the U.S. Department of Housing and Urban Development or the U.S. Veterans Administration where such standards are applicable.

4. Making variances, substitutions or omissions in the construction of on-site residential housing from the schedule of specifications made available for inspection purposes in accordance with the requirements of Part V 8 of this order that are not subject to approval by the U.S. Department of Housing and Urban Development or by the U.S. Veterans Administration and which would significantly reduce the quality of the material or component in which the variance, substitution or omission was made.

5. Making variances, substitutions or omissions in the construction of on-site residential housing where such variance, substitution or omission deviates from approved plans and specifications filed with the U.S. Department of Housing and Urban Development or the U.S. Veterans Administration and which have not been ap-

proved by such agencies with respect to such housing and which would significantly reduce the quality of the material or component in which the variance, substitution or omission was made.

6. Failing to repair, replace or to pay the cost of repairing or replacing any major construction defect or any other defect in accordance with the provisions of respondents' express warranty required under Part III B of this order or in the performance of respondents' obligations under Part VIII of this order within a reasonable time after receipt of written notice of such defect from the purchaser or past purchaser of respondents' on-site residential housing; *provided, however,* that:

(a) Where respondents for any reason are unable to complete such requested repairs within thirty (30) calendar days after receipt of written notice of such defect from the purchaser or past purchaser of respondents' on-site residential housing, respondents shall furnish to such purchaser or past purchaser (as defined in Part VIII) a written statement setting forth the reason or reasons why such requested repairs cannot be undertaken or completed within such thirty day period and a scheduled date on which the requested repairs are, in fact, to be completed within the next sixty (60) day period.

(b) Where respondents are or were prevented from completing repairs by the scheduled date referred to in subparagraph 6(a) above due to intervening circumstances beyond their control, such as labor strike, supplier or subcontractor failure to deliver materials or perform work, or unsuitable weather conditions, such repairs will be completed within a reasonable period of time not to exceed sixty (60) days from the date of the termination of the intervening circumstance.

(c) Where respondents for any reason elect not to honor such request for repairs, respondents shall, within twenty-one (21) calendar days of receiving such request for repairs, notify the purchaser or past purchaser in writing why respondents will not honor the request.

7. Failing to take reasonable steps to insure that all inspections required to be made of each unit of respondents' on-site residential housing by appropriate local and other governmental authorities are, in fact, made at the stage of construction at which such inspections are normally required to be made and retaining copies of such inspection reports for each particular unit of such residential housing and, upon request, making such reports available for inspection by purchasers promptly and without charge.

8. Representing through any means, directly or by implication,

that the land upon which respondents' on-site residential housing is constructed is suitable for the construction of housing unless respondents have performed the necessary site preparation and construction techniques in a manner satisfactory to the U.S. Department of Housing and Urban Development or the U.S. Veterans Administration or to state and local planning and zoning authorities to render the land suitable for residential construction.

9. Representing through any means, directly or by implication, that any of respondents' housing is available for immediate use or occupancy by purchasers or prospective purchasers unless such residential housing units are, in fact, available for immediate use or occupancy.

10. Representing through advertising, advertising depictions or similar means, directly or by implication, that the advertised price for respondents' housing includes as standard items certain features, equipment, architectural design, construction or any other item or characteristic for which respondents in fact make an additional charge; *provided, however,* that nothing in this Paragraph 10 shall prohibit respondents from picturing or depicting a housing unit complete with optional items or characteristics so long as there is a clear and conspicuous disclosure in immediate conjunction therewith that such items or characteristics are available for an additional charge.

11. Representing through any means, directly or by implication, that any room in respondents' housing is suitable for use as a habitable area where such room has not been properly insulated or constructed for such purpose.

12. Representing through the use of the words "for a limited time only" or through any other means or device, directly or by implication, that any change in the price of any of respondents' housing is imminent unless, at the same time and in conjunction therewith, respondents clearly and conspicuously disclose the date such limited time offer expires.

13. Representing through any means, directly or by implication, that sales of respondents' housing to purchasers are free of "closing costs" when in fact such sales do include closing costs, as "closing costs" are hereinabove defined.

14. Representing through any means, directly or by implication, that public schools and housing offered for sale by respondents are or will be located in the same school district unless respondents advise purchasers of the title or office, address and telephone number of the responsible school district authority from whom respondents obtained such information.

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15. Representing through any means, directly or by implication, that respondents' housing is planned, developed, constructed or located with regard to children's recreational needs without disclosing in immediate conjunction therewith the specific means provided or facilities which respondents have constructed to meet the recreational requirements of children.

16. Representing through any means, directly or by implication, the existence of or plans for any educational, recreational, transportation, medical or other facilities adjacent to or in the vicinity of communities in which respondents have built or propose to build their on-site residential housing unless such facility actually exists or, with regard to planned facilities, respondents advise purchasers of the title or office, address and telephone number of the appropriate authority or public official from whom respondents obtained such information.

17. Misrepresenting through any means, directly or by implication, the amount or quality of the topsoil to be furnished to the purchasers of respondents' on-site residential housing.

18. Representing through any means, directly or by implication, that the on-site residential housing purchased from respondents will be taxed at a rate that is lower than the most recent official tax estimate and rate obtained from the officially responsible tax assessing authority, or making any representation relating to the assessed valuation or tax rate of such housing without disclosing the identity or title, address and telephone number of the officially responsible tax assessing authority.

19. Misrepresenting through any means, directly or by implication, that any feature, item of equipment, architectural design, construction, appurtenance or characteristic present in model homes is a standard inclusion in such model or style that will be duplicated in residential housing sold and delivered by respondents to purchasers of such model or style at the advertised or offered price. *Provided, however,* the following will be deemed to be adequate notice to prospective purchasers that such items and features are not included as standard in respondents' on-site residential housing:

(a) A conspicuous sign or signs in or adjacent to the model homes listing items which are optional or unavailable; or

(b) Labels on specific optional and unavailable items; and

(c) Lists available to each prospective purchaser at the entrance of each model home complex which disclose optional and unavailable items; or

(d) Lists in the brochures which describe the particular model or models of respondents' on-site housing which disclose optional and unavailable items.

20. Using beds or mattresses of less than 74-1/2 inches in length as display or decoration in rooms presented as bedrooms in respondents' model homes without conspicuously disclosing by means of a sign in such room (a) that the bed or mattress is shorter than standard size, or (b) the dimensions of the room.

III

A. *It is further ordered,* That respondents, in connection with the advertising, offering for sale or sale of on-site residential housing, shall cease and desist from representing through any means, directly or by implication, that respondents' residential housing is warranted by an express warranty without clearly and conspicuously disclosing:

(a) That the warranty is the standard warranty issued pursuant to the Home Owners Warranty Corporation's national home warranty program, or a warranty substantially identical to such warranty including the specific duration of the warranty;
(b) Or, the following:
(i) The nature and extent of the warranty including disclosure of the parts of said housing that are warranted;
(ii) The specific conditions and limitations of such warranty;
(iii) The specific duration of the warranty;
(iv) The steps that anyone claiming under the warranty must take before respondents fulfill their obligations under the warranty; and
(v) The manner and time in which respondents will perform their obligations under the warranty.

B. *It is further ordered,* That respondents shall furnish purchasers of each unit of respondents' on-site residential housing with a warranty that is substantially identical to the insurer's and the warrantor's undertaking in the Home Owners Warranty Corporation's Home Warranty Agreement (hereafter referred to as the "HOW warranty") currently in use and attached hereto as Appendix A and incorporated by reference in this order, including the procedures for the settlement of disputes; *provided,* that respondents' undertaking for major construction defects shall be for a term of at least four years from the commencement date of each such warranty furnished, and *provided further,* that nothing in this order shall relieve respondents from complying with the Magnuson-Moss Warranty Act, Section 101, *et seq.* (15 USC 2301, *et seq.*), the rules promulgated thereunder, and interpretations issued by the Federal Trade Commission in respect thereto.

C. *It is further ordered,* That in the event disputes arise between respondents and purchasers relating to respondents' liability for defects under Part III B of this order, and such disputes cannot be settled on a mutually agreeable basis within a reasonable period of time not to exceed forty (40) days from the date such dispute arose, then respondents shall notify each such purchaser in writing and at the same time as respondents finally reject the purchaser's claim, that such dispute may be submitted to third-party dispute settlement under the procedures required in Part III B above; *provided,* that purchasers shall not be precluded from exercising rights under the warranty required in Part III B above in respect to making a warranty or insurance claim or filing a demand for dispute settlement at any time prior to the expiration of such forty (40) day period; and, *provided further,* that no later than ten (10) business days excluding Saturdays, Sundays and legal holidays from the receipt of a written request for dispute settlement from purchasers, respondents shall take action to initiate such dispute settlement proceedings.

D. *It is further ordered,* That respondents shall specifically perform in good faith and without unreasonable delay or make payments timely as determined under the dispute settlement procedures required in Part III B above in each instance where the use of such procedures results in a decision in favor of the purchaser subject, however, to such rights under law as either purchaser or respondents may have in connection with the dispute.

IV

It is further ordered, That respondents, directly or indirectly, in connection with the sale of any unit of on-site residential housing, shall not enter into any contracts or employ any other means which prohibit or prevent any purchaser from selecting, within a reasonable length of time, a lending institution of the purchaser's own choice, or that may otherwise have the effect of restricting where the purchaser may seek or secure credit; *provided, however,* nothing contained herein shall prohibit respondents, or any affiliate thereof, from entering into mortgage commitments, mortgages or other similar financing agreements with their purchasers.

V

It is further ordered, That in connection with the advertising, offering for sale or sale of on-site residential housing, respondents shall make available to each and every prospective purchaser who visits respondents' sales offices or model homes a brochure or a written statement relating to such housing that will include the following disclosures in a clear, conspicuous and affirmative manner:

1. For on-site residential housing not covered by the National Flood Insurance Program administered by the U.S. Department of Housing and Urban Development, the identity, address and telephone number of the individual, business firm and government agency that conducted soil tests on land used in the construction of the residential housing offered for sale. In addition, respondents shall require their contractors to state in non-technical language to each prospective purchaser who contacts such contractors whether the land tested is suitable for residential use;
2. The identity or title, address and telephone number of the responsible public school district authority who will furnish information relating to the identity and location of schools for the particular housing unit;
3. Each room or area of the particular housing unit to be purchased that is not insulated to retain the same degree of warmth as rooms designed for use as principal living areas;
4. Each room or area of the particular housing unit to be purchased that is constructed without waterproofing adequate to render such room or area suitable for use as a habitable living area;
5. The most recent official tax rate and estimate obtained from the officially responsible tax assessing authority and the identity or title, address and telephone number of such tax assessing authority;
6. A list containing each and every architectural design, construction feature, appurtenance, optional item or equipment or other characteristic or feature exhibited to the particular purchaser in connection with a model home sample or style offered for sale to such purchaser which characteristic or feature is not included in the model or style of respondents' housing unit offered for sale to such purchaser at the offered or advertised price;
7. A list containing each and every construction feature, appurtenance, optional item or equipment or other characteristic or feature exhibited to the particular purchaser in connection with a model home sample or style offered for sale to such purchaser which characteristic or feature cannot be included or duplicated in the particular housing unit offered for sale to such purchaser even upon the payment of an additional charge because of the style, size, location or any other reason associated with the land or the design of the particular housing unit offered;

8. A notice that plans and specifications for each home being offered for sale are available for inspection by prospective purchasers at respondents' sales offices during normal business hours; *provided,* that such specifications shall include a full description of the materials and components used by respondents in the construction of their on-site residential housing; and, *provided further,* that such description will be satisfied if it substantially includes the type of information contained in the "Description of Materials" disclosure statements required by the United States Federal Housing Administration (FHA Form 2005, as revised from time to time) or the United States Veterans Administration (VA Form 26-1852, as revised from time to time);

9. A notice that purchasers of respondents' housing may select any lending institution of their choice for the purpose of securing a mortgage and are not limited to the lending institution provided by respondents;

10. A statement setting forth respondents' arrangement for repairs and the satisfaction of warranties or in lieu thereof, a copy of the warranty required by Part III B of this order that will be furnished with the housing being offered for sale and a statement of the procedure for the settlement of disputes under such warranty.

VI

It is further ordered, That respondents shall secure a written acknowledgement from each purchaser of respondents' on-site residential housing which shall state the following information:

1. That the disclosures referred to in Paragraph V of this order were received.

2. The date on which the disclosures referred to in Paragraph V of this order were received.

VII

For the purpose of this Part VII, "past purchaser" shall mean the original purchaser of the unit of respondents' on-site residential housing who purchased such unit as new from respondents or from any of respondents' subsidiaries during the period commencing January 1, 1972 and ending on the day immediately preceding the effective date of this order, and who has continued to retain title to such unit as of the effective date of this order.

A. *It is further ordered,* That respondents, in connection with on-site residential housing units sold to past purchasers shall repair, replace, or pay past purchasers the reasonable cost of repair or replacement of defects pursuant to all of the terms, conditions, definitions, approved standards, and exclusions contained in the Home Owners Warranty Corporation Limited Home Warranty Agreement (HOW warranty), which is attached hereto as Appendix A and incorporated by reference herein, when the following conditions exist:

1. In units where respondents transferred title to past purchasers on or after January 1, 1972:

Major construction defects;

2. In units where respondents transferred title to past purchasers within two (2) years prior to the effective date of this order (including the day immediately preceding the effective date of this order):

Major construction defects, or
defects in the plumbing, electrical, heating, or cooling systems due to non-compliance with the approved standards, except defects in appliances, fixtures and items of equipment;

provided, that nothing in this Part VII A shall serve to limit or change respondents' undertaking for remedial action for on-site residential housing units sold and warranted by respondents prior to the effective date of this order with a Home Owners Warranty Corporation's Home Warranty Agreement.

B. *It is further ordered,* That respondents, in connection with the remedial action required by Part VII A of this order, shall:

1. Require all claims by past purchasers for remedial action to be made by affidavit and in the form attached hereto as Appendix C and Appendix D, as applicable and incorporated by reference in this order, and addressed to the office of respondents as designated in the letter of notification required by Part VII C;

2. Process all claims made by past purchasers in the priority in which received at respondents' designated office;

provided, that respondents shall not be required to honor any claim from a past purchaser for remedial action made pursuant to subparagraph 1 hereinabove that is postmarked later than fifty (50) days from the date the letter of notification required by Part VII C of this order is mailed by respondents.

C. *It is further ordered,* That respondents shall, within sixty (60) days from the effective date of this order, mail by United States first class mail to the address of each unit of on-site residential housing sold by respondents during the period January 1, 1972 to the day immediately preceding the effective date of this order, a notification informing past purchasers of respondents' obligations under Part VII of this order, and shall include with such notification affidavit forms for the use of past purchasers in submitting claims for repairs; *provided,* that respondents shall not be required to mail such notification to the address of any unit of on-site residential housing where respondents: 1) prior to the effective date of this order furnished the past purchaser a Home Owners Warranty Corporations' Home Warranty Agreement, or 2) within one year prior to the day immediately preceding the effective date of this order furnished the express warranty attached hereto as Appendix B. Such notification shall also include a clear and conspicuous statement that: Claims from past purchasers for repairs must be postmarked within fifty (50) days from the date of such notification; and disputes concerning respondents' liability for defects may be settled at the past purchaser's option through the procedures described under Part IX 4 of this order. Respondents' notification to past purchasers shall be substantially identical in form and content to the letters of notification attached herewith as Appendix E and Appendix F which are incorporated by reference in this order.

D. *It is further ordered,* That respondents, in connection with claims for repairs received from past purchasers under Part VII A of this order, shall:

1. Respond in writing within forty-five (45) days from the receipt of each past purchaser's affidavit which asserts a claim for repairs. Such response shall include a scheduled date for the completion of the repairs which date shall not be unreasonably distant in the future; or, if any repair is not to be made, a full and complete explanation, including a technical explanation as applicable, of the reason or reasons why respondents will not make the requested repairs; and shall be signed by a responsible official of Kaufman and Broad, Inc.;

2. Complete all repairs which respondents agree to make no later than the scheduled date referred to in subparagraph D1 above; *provided, however,* that in the event respondents are prevented from completing repairs by such date due to intervening circumstances beyond their control such as labor strike, supplier failure to deliver materials or unsuitable weather conditions, such repairs will be completed within a reasonable period of time not to exceed sixty (60) days from the date of the termination of the intervening circumstance and respondents shall notify each such past purchaser, in writing, of the reason or reasons for the delay.

E. *It is further ordered,* That respondents shall:

1. Within sixty (60) days from the effective date of this order, submit to the Chicago Regional Office of the Federal Trade Commission the affidavit of an officer of respondent Kaufman and Broad, Inc. which sets forth the date, manner and form by which past purchasers were notified by respondents as required under Part VII C of this order.

2. At six month intervals for a period of two years following the effective date of this order, submit the certified statement of an independent contractor who is acceptable to the Commission showing the specific manner and form in which respondents are complying and have complied with each provision of Part VII of this order.

VIII

For the purpose of this Part VIII, "past purchaser" shall mean the purchaser of a unit of respondents' on-site residential housing who, as of the effective date of this order, holds title to a unit covered by an unexpired term of respondents' one year express warranty, a copy of which is attached hereto as Appendix B.

It is further ordered, That respondents, in connection with on-site residential housing units sold to past purchasers, shall repair, replace, or pay past purchasers the reasonable cost of repair or replacement of defects covered by respondents' express warranty or when the following conditions exist:

[a] Major construction defects;

[b] defects in the plumbing, electrical, heating or cooling systems due to non-compliance with the approved standards;

[c] other defects due to non-compliance with the approved standards; or

[d] defects in appliances, fixtures and items of equipment due to non-compliance with the approved standards or for the term of the manufacturer's written warranty, if respondents' have assigned the manufacturer's warranty to past purchasers, but not to exceed one year.

IX

It is further ordered, That respondents, in connection with respondents' obligations under Part VII and Part VIII of this order to take remedial action for defects, shall:

1. Make repairs in accordance with the approved standards;

2. Make repairs in a workmanlike manner, and with materials or components identical to, or of an equal or better grade or quality than, the materials or components used in the original construction of the particular on-site residential housing unit;

3. Offer to purchase each past purchaser's unit at the repurchase price if the defects cannot be remedied within a reasonable time;

4. In each instance where a dispute arises between respondents and a past purchaser relating to respondents' obligations to take remedial action for defects, and such dispute cannot be settled on a mutually agreeable basis within a reasonable period of time not to exceed forty (40) days from the date such dispute arose, then respondents shall offer in writing to each such past purchaser and at the same time as respondents finally reject the past purchaser's claim, to submit such dispute to dispute settlement procedures which are substantially identical to the dispute settlement procedures described on page 6 of the "HOW warranty" attached hereto as Appendix A and shall include with such offer a form such as the "Demand for Dispute Settlement" which appears as page 9 of such "HOW warranty"; *provided,* that no later than ten (10) business days excluding Saturdays, Sundays and legal holidays from the receipt of such written request for dispute settlement from past purchasers, respondents shall take action to initiate such dispute settlement proceedings.

5. Specifically perform in good faith and without unreasonable delay or make payments timely in each instance where the use of the procedures described in subparagraph 4 hereinabove results in a decision in favor of the past purchaser, subject, however to such rights under law as either purchaser or respondents may have in connection with the dispute;

6. Preserve, for a period of no less than three (3) years from the effective date of this order the original document, or copies thereof as appropriate, and upon reasonable notice provide access to the Commission or its representatives for the purpose of inspection and copying, all documents, reports and records including all requests for repairs and correspondence relating to compliance with Part VII and Part VIII of this order.

X

It is further ordered, That the respondents shall maintain and, upon reasonable notice, provide access to the Commission or its representatives for the purpose of inspection and copying, for a period of three (3) years from the date of transfer of title by respondents of each unit of on-site residential housing:

1. All inspection reports made by local and other governmental authorities during the construction of respondents on-site residential housing pursuant to Paragraph II 7 of this order.

2. All complaints and requests for repairs made to respondents by purchasers of such on-site residential housing under the provisions of respondents' express warranties.

3. All correspondence and documents regarding complaints and requests for repairs made to respondents by purchasers of such on-site residential housing under the provisions of respondents' express warranties.

4. All written acknowledgements received from purchasers of respondents' on-site residential housing pursuant to Paragraph VI of this order.

XI

It is further ordered, That no provision of this order shall be construed in any way to annul, invalidate, repeal, terminate, modify or exempt respondents from complying with agreements, orders, rules or building codes or directives of any kind issued or required by any governmental agency, or any federal, state or local laws, or act as a defense to actions instituted by municipal, state or federal regulatory agencies; *provided,* that if federal law hereafter enacted or federal regulation hereafter promulgated requires respondents to furnish a warranty for on-site residential housing and such warranty is less restrictive than the corresponding provisions of the warranty required under Part III B of this order, and respondent files a motion with the Federal Trade Commission to modify this order to correspond to such less restrictive other warranty, the Federal Trade Commission shall rule upon respondents' motion within 120 days after such motion is filed or, if respondents' motion to modify is filed at least 60 days prior to the effective date of such law or regulation, then the Federal Trade Commission shall rule upon respondents' motion within 60 days after the effective date of such law or regulation and; *provided further,* that should the Federal Trade Commission fail to rule upon respondents' motion to modify within such time periods, then such law or regulation shall automatically be deemed to modify and replace the corresponding provision(s) of this order.

XII

It is further ordered, That respondents shall within thirty (30) days of the effective date of this order distribute a copy of this order to:

1. Each of respondents' operating divisions and subsidiaries in the United States.

2. All officers and employees of the respondent corporations and of the operating divisions and subsidiaries of all of respondents' corporations in the United States who are engaged or who may hereafter become engaged in the production, advertising, offering for sale or sale of respondents' on-site residential housing.

3. Each of the advertising agencies, interior designers, consulting firms or other independent contractors in the United States who are engaged or who may hereafter become engaged in the decorating of respondents' model home samples, or in the creation or placement of advertising in connection with the offering for sale of respondents' on-site residential housing.

It is further ordered, That respondents notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondents such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporations which may affect compliance obligations arising out of the order.

It is further ordered, That the respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

APPENDIX A

Warranty No.

LIMITED WARRANTY
HOME WARRANTY AGREEMENT

1. Builder's Name and Address: ______________________

____

2. Purchaser's Name: ______________________

3. Address of Home: ______________________

____

4. Purchase Price of Home: $ ______________________

5. Commencement Date (first occupancy or final settlement, whichever occurs first): ______________________

6. Common Elements Commencement Date (condominiums only, date the first unit in the structure was occupied or its title transferred, whichever occurred first): ______________________

7. Local HOW Council (name, address and phone number): ______________________

____

8. National HOW Council: Home Owners Warranty Corporation, 15th & M Streets, N.W., Washington, D.C. 20005, and its successors and assigns.

9. Insuror: American Bankers Insurance Company of Florida and its successors and assigns.

10. ☐Check this box if an Addendum is attached to this Home Warranty Agreement listing items of material or work which are excluded from this Agreement because they were not provided by the Builder and they are not included in the purchase price of home.

The Purchaser and Builder have signed this Agreement on this _______ day of ______________, 19___.

BUILDER: PURCHASER(S):

______________________ ______________________
(Insert Name of Builder)

By: ______________________ ______________________

CONSEQUENTIAL DAMAGES

Consequential damages are excluded. (Some states do not allow the exclusion or limitation of consequential damages so the above limitation or exclusion may not apply to you).

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IMPORTANT NOTICE – PLEASE READ

- The Builder has arranged for insurance coverage, described on page 5 of this agreement. The insurance coverage will be officially extended to you by a "Certificate of Participation" (or insurance policies) which will be sent to you after you sign this agreement. If you do not receive your Certificate of Participation or policies within 6 weeks, contact your Local HOW Council.

- You and the Builder should sign this agreement at final settlement. This agreement should be executed only after substantial completion of the home by the Builder and inspection of the home by the Purchaser.

- Neither this agreement nor the insurance coverage cover failure of the Builder to complete construction.

- At the time you receive this agreement the Builder will give you a set of the Approved Standards which are part of this warranty and which the Builder is obligated to meet under this agreement.

LIMITED WARRANTY

Identity of Warrantor. The Builder named on page 1 is the warrantor under this warranty.

To Whom Given. This warranty is extended to you as Purchaser (the first owner to occupy the home as a residence for yourself or your family) and automatically to any subsequent owners of the home and any mortgage lender who takes possession of the home (see exclusion during non-residential use, page 5).

Coverage During First Year. For one year, beginning on the commencement date filled in on page 1, the Builder warrants that the home will be free from defects due to noncompliance with the Approved Standards and from major construction defects.

A "major construction defect" is actual damage to the load-bearing portion of the home (including damage due to subsidence, expansion or lateral movement of soil from causes other than flood or earthquake) which affects its load-bearing function and which vitally affects (or is imminently likely to produce a vital effect on) the use of the home for residential purposes.

Coverage For Up to One Year. The Builder warrants that all appliances, fixtures and items of equipment will be free from defects due to noncompliance with the Approved Standards for one year or for the term of the manufacturer's written warranty (if a manufacturer's written warranty is assigned to you by the Builder), whichever is less.

Coverage During Second Year. During the second year after the commencement date, the Builder continues to warrant that the home will be free from major construction defects and that the plumbing, electrical, heating, and cooling systems will perform according to the Approved Standards, unless their failure is the result of a defect in an appliance, fixture, or item of equipment. (See the Approved Standards for definitions).

Coverage of Common Elements in Condominiums. Common elements serving condominium units are also covered by this warranty. "Common elements" mean any structural portion of a condominium structure (including, but not limited to, any passageways, rooms or other spaces) which are provided for the common use of the residents of the structure. It also means part of a mechanical, electrical, heating, cooling or plumbing system serving two or more condominium units and outbuildings containing parts of such a system.

Common elements are covered for the same length of time as similar items which are part of an individual unit, but the beginning date of the warranty period on common elements is determined by the common elements commencement date on page 1.

Builder's Performance. If a defect occurs in an item which is covered by this warranty, the Builder will repair, replace, or pay you the reasonable cost of repairing or replacing the defective item. The Builder's total liability under this warranty is limited to the purchase price of the home filled in on page 1. The choice among repair, replacement or payment is the Builder's. Steps taken by the Builder to correct defects shall not act to extend the terms of this warranty.

Other Insurance. In the event the Builder repairs or replaces, or pays the cost of repairing or replacing, any defect covered by this warranty for which you are covered by other insurance, you must, upon request by the Builder, assign the proceeds of such insurance to the Builder to the extent of the cost to the Builder of such repair or replacement.

Other Rights. This warranty gives you specific legal rights. You may also have other legal rights which vary from state to state. This agreement does not affect any rights of you or the Builder under any other express or implied warranty.

INSURANCE COVERAGE

Assignment of Insurance Coverage. The Builder hereby assigns the insurance coverage to you, but your insurance protection becomes effective only when you receive your Certificate of Participation or policies. Once you receive your Certificate or policies your insurance will cover any defects back to the time of the commencement date(s) filled in on page 1.

Scope of Insurance Coverage. The insuror, subject to a one time $50.00 deductible, will meet all the Builder's obligations under this warranty as set forth in this agreement if, after completion of arbitration, the Builder for any reason fails to meet them. The insuror will directly insure against major construction defects for an additional eight years (beginning two years after, and ending ten years after, the appropriate commencement date). The total liability of the insuror during the ten years covered by this agreement is limited to the purchase price filled in on page 1.

Expenses. The insurance coverage includes actual, reasonable shelter expenses during repairs.

EXCLUSIONS

The following are not covered by either the warranty or the insurance coverage:

1. Defects in outbuildings (except that outbuildings which contain the plumbing, electrical, heating, or cooling systems serving the home are covered), swimming pools and other recreational facilities; driveways; walkways; patios; boundary walls; retaining walls which are not necessary for the home's structural stability; fences; landscaping (including sodding, seeding, shrubs, trees and plantings); off-site improvements; or any other improvements not a part of the home itself.

2. Bodily injury, damage to personal property, or damage to real property which is not part of the home which was included in the purchase price filled in on page 1.

3. Any damage to the extent it is caused or made worse by:

- Negligence, improper maintenance or improper operation by anyone other than the Builder or his employees, agents or subcontractors; or
- failure of anyone other than the Builder or his employees, agents or subcontractors to comply with the warranty requirements of manufacturers of appliances, equipment or fixtures; or
- failure to give notice to the Builder of any defect within a reasonable time; or
- changes of the grading of the ground by anyone other than the Builder, or his employees, agents or subcontractors.

4. Any defect in, or caused by, materials or work (including, but not limited to, items shown on any attached "Addendum to Home Warranty Agreement") supplied by anyone other than the Builder, or his employees, agents or subcontractors.

5. Normal wear and tear or normal deterioration.

6. Accidental loss or damage from causes such as, but not limited to: fire, explosion, smoke, water escape, changes which are not reasonably foreseeable in the level of the underground water table, glass breakage, wind storm, hail, lightning, falling trees, aircraft, vehicles, flood and earthquake. However, soil movement (from causes other than flood or earthquake) is not excluded.

7. Insect damage.

8. Any loss or damage which arises while the home is being used primarily for non-residential purposes.

9. Any defect which does not result in actual loss or damage.

HOW TO MAKE A WARRANTY CLAIM

Submission of Claims to Builder. If you have a complaint, you should first send a clear and specific written complaint to the Builder. You may also wish to provide the Local HOW Council with a copy of any such complaint for its information.

Time of Notice of Claim. Written notice of a defect in any item under the warranty must be received by the Builder (or, at your option, the Local HOW Council) within 30 days after the warranty on that item expires.

Demand for Dispute Settlement. If you and the Builder disagree concerning the warranty obligations under this agreement (or he does not respond to your complaint), you may request informal dispute settlement concerning your claim by mailing the "Demand for Dispute Settlement" form (see back page) to the Local HOW Council. You may also request informal dispute settlement by submitting a letter specifically requesting dispute settlement and identifying yourself, the Builder, the home, the defects claimed and the remedies sought.

Conciliation and Arbitration. HOW provides for conciliation and for nonbinding arbitration conducted by the American Arbitration Association under its Expedited Home Construction Arbitration Rules (or by another approved organization). No fee or deposit is required. No arbitration decision may call for performance beyond the scope of the warranty provided in this agreement.

After it receives your "Demand for Dispute Settlement" form, the Local HOW Council will assign a conciliator, who will attempt to work out a voluntary conciliation agreement between you and the Builder as to the settlement of your claim. After you have attempted conciliation, you may demand arbitration of any unresolved warranty dispute between you and the Builder.

You are not required to submit your claim to dispute settlement unless you wish to do so. However, under Public Law 93-637 you may not file suit against the Builder until you have submitted your claim and a decision has been reached. Suit may be permitted under other state or federal laws and you are only required to wait for a decision for 40 days (47 if you do not contact the builder before filing a claim) after which time you may sue. In addition, the insuror is not required to pay you under the insurance coverage unless you complete arbitration.

Acceptance of Decision. If you decide to accept the decision you must sign and return to the Local HOW Council, within 45 days after the date of the decision, an "Acceptance of Decision" form by which you agree to accept the arbitrator's decision in full satisfaction of your claim. The Builder will then be bound to perform as required in the decision. The Builder is not responsible for damage caused or made worse by your delay in accepting the decision.

The time allowed by the decision for the Builder's performance will be measured from the date the Local HOW Council receives your "Acceptance of Decision" form and will be extended automatically if weather, strikes, or other matters not within the Builder's control interfere with his performance.

Rejection of Decision. After you receive the decision, you must decide whether or not to accept it. You may reject the decision in which case it has no legal effect on you.

If you do not accept the decision, the Builder is under no obligation to perform in accordance with the decision.

Condominium Claims. If the claim involves a common element in a condominium, it may be made only by an authorized representative of the condominium association.

Other Claimants. Any other person to whom the warranty is extended should submit and pursue any claims that he may have by the same procedures.

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HOW TO MAKE AN INSURANCE CLAIM

If a claim arises under the warranty and the Builder cannot or will not cooperate in HOW dispute settlement procedures, the Local HOW Council will contact the insuror and the insuror will (if it disputes the claim) take the place of the Builder in the dispute settlement procedures and perform as directed by the decision.

If the Builder cooperates in HOW dispute settlement procedures, but fails to perform as directed within the time specified, you should notify your Local HOW Council, which will arrange with the insuror for performance of the warranty obligations under the decision.

If a claim arises with respect to the direct insurance against major construction defects during the third through tenth years after the commencement date(s) of this agreement, you should notify your Local HOW Council, which will arrange with the insuror to investigate the claim. If the insuror disputes the claim, you may request arbitration. The insuror has agreed to be bound by the arbitrator's decision, subject to the following paragraph.

Prerequisite to Payment by Insuror. The insuror will not pay a claim until you have completed arbitration and accepted the decision (unless the insuror chooses not to dispute the claim), and have signed and delivered a release of all rights you may have against the insuror arising out of the specific claim, and, in the case of a claim arising under the first two years' coverage, until you have signed and delivered to your Local HOW Council an assignment to the insuror of your claim against the Builder.

HOW Not a Warrantor or an Insuror. The National HOW Council and the Local HOW Council are not warrantors or insurors. Only the insuror named on page 1 is responsible for paying claims under the insurance coverage.

MISCELLANEOUS

Representations by Builder. The Builder hereby represents to you that he is registered with the Local HOW Council and the home has been initially enrolled with the Local HOW Council; that he is the person, corporation, partnership or other entity which conveys title to the home to you or by contract builds the home on your land or land owned by a third party, and he is, therefore, entitled to sign this agreement; that the home qualifies for the insurance coverage; and that he knows of no reason why the Certificate of Participation (or insurance policies) should not be issued to you.

Assignment of Manufacturers' Warranties. The Builder hereby assigns to you all manufacturers' warranties on items he has provided as part of the home.

Independence from Purchase Contract. This agreement is independent of the contract between you and the Builder for the construction of the home and/or its sale to you. Contract disputes which are not warranty disputes are not eligible for HOW arbitration, for the insurance coverage or for other settlement under this agreement. Nothing contained in that contract or any other contract between you and the Builder can restrict or override the provisions of this agreement. You and the Builder may contract for additional standards or requirements, but only the Approved Standards are applicable under this agreement and the Certificate of Participation (or insurance policies).

Notices. All notices to the Builder, to you, to your Local HOW Council or to the National HOW Council must be sent by mail, postage prepaid, to the recipient at the address shown for the recipient on page 1, or to whatever other address the recipient may designate in writing.

General Provisions. Should any provision of this agreement be deemed by a court of competent jurisdiction to be unenforceable, that determination will not affect the enforceability of the remaining provisions. This agreement is to be binding upon the parties, their heirs, executors, administrators, successors and assigns. Use of one gender in this agreement includes all other genders; and use of the plural includes the singular, all as may be appropriate. This agreement is to be covered by and construed in accordance with the laws of the state in which the home is located.

Amendments. This agreement cannot be changed or altered in any way.

DEMAND FOR DISPUTE SETTLEMENT

TO THE OWNER: Complete the following and mail to the Local HOW Council at the address shown on the front page of your Home Warranty Agreement. If some of the requested information is unknown to you, please indicate.

1. Name of Owner(s): ______
2. Address: ______
3. Home Warranty Agreement Number: ______
4. Date of Home Warranty Agreement: ______
5. Name of Builder: ______
6. Describe Defects:

(Use additional sheets, if necessary)

7. Remedy Sought:

(Use additional sheets, if necessary)

The undersigned owner(s) of the home covered by the Home Warranty Agreement noted above hereby demands that the Local HOW Council undertake to arrange for conciliation of his (their) dispute with the above named Builder. The owner(s) understands that at any time after conciliation has been attempted, he (they) can end conciliation and demand that arbitration be initiated.

______ Signature ______ Date

______ Signature ______ Date

Do Not Write Below This Line

TO THE BUILDER: You are hereby notified that the above Demand for Dispute Settlement has been filed with Home Owners Warranty Council of ______.
The time and location of the hearing will be arranged by the conciliator appointed by the Local HOW Council.

Approved Standards

ATTACH TO EVERY
HOME WARRANTY AGREEMENT

HOW
HOME
OWNERS
WARRANTY
CORPORATION

Introduction

The approved standards are the required standards for construction of all Homes built under the Home Owners Warranty Program. Compliance with these standards is the basis for acceptance of the Home under the Warranty Program and issuance of the Certificate of Participation in the Home Warranty Insurance Policy.

These standards consist of two parts:

(a) Those standards regulating the structural, mechanical-plumbing, and electrical systems which apply during the applicable Initial Warranty Period, and

(b) Quality Standards which establish minimum performance standards relating to specific deficiencies which apply during the applicable Initial Warranty Period.

If there is any conflict between (a) and (b) above, the higher standard shall govern.

Builder responsibility under these standards does not extend to items which have been subject to owner neglect, modification or abnormal use.

Structural, Mechanical-Plumbing, and Electrical Standards

I. The structural, mechanical-plumbing, and electrical standards shall be those contained in the Building Code, Mechanical-Plumbing Code and Electrical Code regulating that respective construction in the area. Inspection by the governmental jurisdiction will provide evidence of compliance.

II. In the case where no Codes exist or where the existing codes are found not completely acceptable, one of the following will apply:

(A) The Minimum Property Standards of the U.S. Department of Housing and Urban Development with inspection by HUD, VA, or FmHA personnel.

(B) A combination of the following Model Codes to cover building, mechanical-plumbing, and electrical:

BUILDING CODES

Boca Basic Building Code
Building Official & Code
Administrators International, Inc.

National Building Code
American Insurance Association

Southern Standard Building Code
Southern Building Code Congress

Uniform Building Code
International Conference of Building
Officials

One And Two Family Dwelling Code
Under the National Recognized
Model Codes

MECHANICAL CODES

Uniform Building Code, Volume II,
Mechanical
International Conference of
Building Officials

Boca Basic Mechanical Code
Building Official & Code
Administrators International, Inc.

Southern Standard Mechanical Code
Southern Building Code Congress

PLUMBING CODES

Southern Standard Plumbing Code
Southern Building Code Congress

Uniform Plumbing Code
International Association of
Plumbing & Mechanical Officials

Boca Plumbing Code
Building Official & Code
Administrators International, Inc.

ELECTRICAL CODES

Electrical Code For One And
Two Family Dwellings
National Fire Protection Association

National Electrical Code
National Fire Protection Association

Inspection will be provided by inspectors under the control of the Local Council.

(C) The codes of a nearby jurisdiction. Inspection will be made either by persons under the control of the Local Council or by arrangement with the nearby jurisdiction.

SYSTEMS AND APPLIANCES, FIXTURES AND EQUIPMENT

For the purpose of the Home Warranty Agreement, the Certificate of Participation and these Approved Standards, the items below have the following meaning:

I. Appliances, Fixtures and Equipment.

Appliances, Fixtures and Equipment (including their fittings, attachments, controls and appurtenances) shall include, but not be limited to, furnaces, humidifiers, air purifiers, air handling equipment, ventilating fans, air conditioning condensers and compressors, water heaters, pumps, stoves, refrigerators, garbage disposals, compactors, dishwashers, automatic garage door openers, washers and dryers, bathtubs, sinks, commodes, faucets and fittings, light fixtures, light switches, convenience outlets, circuit breakers, thermostats and controls.

The Initial Warranty Period for Appliances, Equipment and Fixtures (including their fittings, attachments, controls and appurtenances) for which there is no written manufacturer's warranty, shall be one year.

II. Systems.

Systems (exclusive of Appliances, Fixtures and Equipment) mean the following:

(A) Plumbing System—all pipes and their fittings, including septic tanks and their pipe fields.

(B) Electrical System—all wiring and connections, including electrical boxes.

(C) Heating and Cooling Systems—all duct work, steam and water pipes, refrigerant lines, registers, convectors and dampers.

Quality Standards

The Quality Standards are intended to specify the minimum performance standards for construction of Homes and to set forth the basis for determining the validity of all home buyer complaints related to defective materials and workmanship during the applicable initial Warranty Period under the Home Owners Warranty Program.

Only the most frequent defects of concern to the home buyer have been enumerated in the Quality Standards set forth in the pages that follow. If a specific defect has not been enumerated, this indicates only that a performance standard for such defect has not yet been adopted by the Local Council and approved by the National Council.

To the extent that minimum performance standards for construction have not been enumerated in these Quality Standards, Builders shall construct Homes in accordance with good industry practice which assures quality of materials and workmanship. Likewise, the validity of any home buyer complaints for defects for which a standard has not been enumerated herein shall be determined on the basis of good industry practice which assures quality of materials and workmanship, and any conciliation or arbitration of such complaints shall be conducted accordingly.

The following Quality Standards are expressed in terms of performance standards. Non-compliance with the performance standard calls for corrective action by the Builder. The format is designed for easy comprehension by both layman and Builder as follows:

1. *Possible Deficiency*—a brief statement in simple terms of the problems to be considered.

2. *Performance Standard* — a performance standard relating to a specific deficiency.

3. *Builder Responsibility*—a statement of the corrective action required of the Builder to repair the deficiency or any other damage resulting from making the required repair.

2. SITE WORK

02220 EXCAVATING AND BACKFILLING

Possible Deficiency: Settling of ground around foundation, utility trenches or other filled areas.

Performance Standard: Settling of ground around utility trenches or other filled areas, maximum allowable 6 inches. Settling of backfill around foundation shall not interfere with water drainage away from the house.

Builder Responsibility: Upon request by the buyer, the builder shall fill excessively settled areas one time only during the first year of warranty. The owner shall be responsible for any grass, shrubs or other landscaping affected by placement of such fill.

02500 SITE DRAINAGE

Possible Deficiency: Improper drainage of the site.

Performance Standard: The necessary grades and swales should be established to insure proper drainage away from the house. No standing water should remain in the yard 24 hours after a rain, except swales which may drain as long as 48 hours after a rain, or sump pump discharge. No grading determination shall be made while there is frost in the ground.

Builder Responsibility: The builder is responsible only for establishing the proper grades and swales. The owner is responsible for maintaining such grades and swales once they have been properly established by the builder.

3. CONCRETE

03300 CAST-IN-PLACE CONCRETE
(Non-Structural)

Possible Deficiency: Basement or foundation wall cracks.

Performance Standard: Non-Structural cracks are not unusual in concrete foundation walls. Such cracks greater than 1/8 inch in width are considered excessive.

Builder Responsibility: The Builder shall repair non-structural cracks in excess of 1/8 inch by surface patching. These repairs should be made toward the end of the first year of ownership to permit normal settling of the home to stabilize.

Possible Deficiency: Cracking of basement floor.

Performance Standard: Minor cracks in concrete basement floors are common. Cracks exceeding 3/16 inch width or 1/8 inch in vertical displacement are considered excessive.

Builder Responsibility: Builder should repair cracks exceeding maximum tolerances by surface patching or other methods as required.

Possible Deficiency: Cracking of attached garage slab.

Performance Standard: Cracks in garage slabs in excess of 1/4 inch in width or 1/4 inch in vertical displacement are considered excessive.

Builder Responsibility: Builder shall repair excessive cracks as required.

Possible Deficiency: Cracking, settling, or heaving of stoops or steps.

Performance Standard: Stoops or steps should not settle or heave in excess of 1 inch in relation to the house structure. No cracks except hairline cracks (less than 1/16 inch) are acceptable in concrete stoops.

Builder Responsibility: Builder shall take whatever corrective action is required to meet acceptable standards.

Possible Deficiency: Cracks in attached patios.

Performance Standard: Cracks in excess of 1/4 inch width or in vertical displacement are considered excessive.

Builder Responsibility: Builder to repair as required.

Possible Deficiency: Pitting, scaling or spalling of concrete work.

Performance Standard: Concrete surfaces should not disintegrate to the extent that the aggregate is exposed under normal conditions of weathering and use.

Builder Responsibility: Builder to take whatever corrective action is necessary to repair or replace defective concrete surfaces. The builder is not responsible for deterioration caused by salt, chemicals, mechanical implements and other factors beyond the builder's control.

Possible Deficiency: Excessive powdering or chalking of concrete surface.

Performance Standard: Powdering or chalking of concrete surfaces is not permissible, but should not be confused with surface dust.

Builder Responsibility: The builder shall take whatever corrective action is necessary to repair or resurface defective areas.

Possible Deficiency: Standing water on stoops.

Performance Standard: Water should drain from outdoor stoops and steps.

Builder Responsibility: The builder shall take corrective action to assure proper drainage of stoops and steps.

Possible Deficiency: Cracks in concrete slab-on-grade floors.

Performance Standard: Cracks which significantly impair the appearance or performance of the finish flooring material shall not be acceptable.

Builder Responsibility: The builder shall repair cracks as necessary so as not to be readily apparent when the finish flooring material is in place.

4. MASONRY

04200 UNIT MASONRY (Non-Structural)

Possible Deficiency: Basement or foundations wall cracks.

Performance Standard: Small non-structural cracks are not unusual in mortar joints of masonry foundation walls. Such cracks greater than ⅛ inch in width are considered excessive.

Builder Responsibility: The builder shall repair non-structural cracks in excess of ⅛ inch by surface patching. These repairs should be made toward the end of the first year of ownership to permit normal settling of the home to stabilize.

Possible Deficiency: Cracks in masonry walls or veneer.

Performance Standard: Small cracks are common in mortar joints of masonry construction. Cracks greater than ⅛ inch in width are considered excessive.

Builder Responsibility: Repair cracks in excess of ⅛ inch by surface pointing. These repairs should be made toward the end of the warranty period to permit normal settling of the home to stabilize.

6. WOOD AND PLASTICS

06100 ROUGH CARPENTRY

Possible Deficiency: Floors squeak.

Performance Standard: Should not be objectionable to the owner within reasonable repair capability.

Builder Responsibility: Locate problem and correct.

Possible Deficiency: Uneven floors.

Performance Standard: Floors should not be more than ¼ inch out of level within any 32 inch measurement. Floor slope within any room shall not exceed 1/240 of the room width.

Builder Responsibility: Builder to correct or repair to meet the above standard.

06200 FINISH CARPENTRY—INTERIOR

Possible Deficiency: Quality of interior trim workmanship.

Performance Standard: Joints in moldings or joints between moldings and adjacent surfaces should not result in cracks exceeding ⅛ inch in width.

Builder Responsibility: Repair defective joints.

FINISH CARPENTRY—EXTERIOR

Possible Deficiency: Quality of exterior trim workmanship.

Performance Standard: Joints between exterior trim elements, including siding, should not result in open cracks in excess of ¼ inch. In all cases the exterior trim and siding shall be capable of performing its function to exclude the elements.

Builder Responsibility: Builder to repair open cracks.

7. THERMAL AND MOISTURE PROTECTION

07100 WATERPROOFING

Possible Deficiency: Leaks in basement or foundation.

Performance Standard: No leaks resulting in actual trickling of water are acceptable. However, leaks caused by improper landscaping installed by owner, or failure of owner to maintain proper grades are not covered by the warranty. Dampness of the walls is often common to new construction and is not considered a deficiency.

Builder Responsibility: The builder shall take such action as necessary to correct base-leaks except where the cause is determined to result from owner negligence.

07300 SHINGLES AND ROOFING TILES

Possible Deficiency: Roof or flashing leaks.

Performance Standard: Roofs or flashing should not leak under normally anticipated conditions.

Builder Responsibility: The builder shall correct or repair any verified roof leaks.

07460 CLADDING/SIDING

See 06200.

07500 MEMBRANE ROOFING

See 07300.

07600 FLASHING AND SHEET METAL

See 07300.

07900 SEALANTS

Possible Deficiency: Leaks in exterior walls due to inadequate caulking.

Performance Standard: Joints and cracks in exterior wall surfaces and around openings should be properly caulked to exclude the entry of water. Properly installed caulking will shrink and must be maintained by the homeowner within the life of the home after the first year of warranty.

Builder Responsibility: Builder shall repair and/or caulk joints or cracks in exterior wall surfaces as required to correct deficiency.

8. DOORS AND WINDOWS

08200 WOOD DOORS

Possible Deficiency: Warpage of interior passage and closet doors.

Performance Standard: Interior doors (full opening) should not warp to exceed National Woodwork Manufacturers Association standards (¼ inch).

Builder Responsibility: Correct or replace and refinish defective doors to match existing doors as nearly as possible.

Possible Deficiency: Warpage of exterior doors.

Performance Standard: Exterior wood doors should not warp to exceed National Woodwork Manufacturers Association Standards (¼ inch).

Builder Responsibility: Correct or replace and refinish inoperable or poorly fitting doors.

08300 GARAGE DOORS

Possible Deficiency: Garage door fails to operate properly.

Performance Standard: Garage doors should operate properly under normal conditions of use.

Builder Responsibility: The builder shall correct or adjust garage doors as required.

08500 METAL WINDOWS

Possible Deficiency: Malfunction of windows.

Performance Standard: Windows should operate with reasonable ease as intended.

Builder Responsibility: Builder to correct or repair as required.

08600 WOOD AND PLASTIC WINDOWS

See 08500.

98730 WEATHER STRIPPING AND SEALS

Possible Deficiency: Drafts around doors and windows.

Performance Standard: Some infiltration is normally noticeable around doors and windows, especially during high winds. Excessive infiltration resulting from open cracks, poorly fitted doors or windows, or poorly fitted weather stripping is not permissible.

Builder Responsibility: The builder shall adjust or correct open cracks, poorly fitted windows or doors, or poorly fitted weather stripping.

9. FINISHES

09100 LATH AND PLASTER

Possible Deficiency: Cracks in stucco wall surfaces.

Performance Standard: Hairline cracks are not unusual in stucco walls surfaces. Cracks greater than ⅟₁₆ inch in width are considered excessive.

Builder Responsibility: The builder shall repair cracks exceeding ⅟₁₆ inch as required

09100 LATH AND PLASTER and
09250 GYPSUM WALLBOARD

Possible Deficiency: Defects caused by poor workmanship such as blisters in tape, excess compound in joints, cracked corner beads, or trowel marks.

Performance Standard: Slight defects such as nail pops, seam lines and cracks are common in plaster and gypsum wallboard installations. However, obvious defects of poor workmanship resulting in blisters in tape or excess compound in joints, trowel marks and cracked corner beads are not acceptable.

Builder Responsibility: Correct such defects to acceptable tolerance.

09310 CERAMIC TILE

Possible Deficiency: Ceramic tile cracks or becomes loose.

Performance Standard: Ceramic tile should not crack or become loose.

Builder Responsibility: The builder shall replace any cracked tiles and resecure any loose tiles unless the defects were caused by the owner's negligence.

Possible Deficiency: Cracks appear in grouting of ceramic tile joints or at junctions with other material such as a bathtub.

Performance Standard: Cracks in grouting of ceramic tile joints are commonly due to normal shrinkage conditions. Regrouting of these cracks are a maintenance responsibility of the homeowner within the life of the home after the first year of warranty.

Builder Responsibility: Will repair grouting as necessary one time within the first year of warranty.

09650 RESILIENT FLOORING

Possible Deficiency: Nail pops appear on the surface of resilient flooring.

Performance Standard: Readily apparent nail pops should be repaired.

Builder Responsibility: The builder shall repair or replace resilient floor covering with similar material. Builder is not responsible for discontinued patterns or color variation in the floor covering.

Possible Deficiency: Depressions or ridges appear in the resilient flooring due to subfloor irregularities.

Performance Standard: Readily apparent depressions or ridges exceeding ⅛ inch should be repaired. The ridge or depression measurement is taken as the gap created at one end of a six-inch straight edge placed over the depression or ridge with three inches on one side of the defect held tightly to the floor.

Builder Responsibility: The builder shall take corrective action, as necessary to bring the defect within acceptable tolerances so that it is not readily visible. Builder is not responsible for discontinued patterns or color variations in floor covering.

Possible Deficiency: Resilient flooring loses adhesion.

Performance Standard: Resilient flooring should not lift, bubble, or become unglued.

Builder Responsibility: The builder shall repair or replace resilient flooring as required. The builder shall not be responsible for discontinued patterns or color variation of floor covering.

Possible Deficiency: Seams or shrinkage gaps show at resilient flooring joints.

Performance Standard: Gaps shall not exceed ⅛ inch in width in resilient floor covering joints. Where dissimilar materials abut, a gap not to exceed ⅛ inch is permissible.

Builder Responsibility: The builder shall take action as necessary to correct the problem.

09900 PAINTING

Possible Deficiency: Exterior paint or stain peels or deteriorates.

Performance Standard: Exterior paints or stains should not fail during the first year of ownership.

Builder Responsibility: Builder shall properly prepare and refinish affected areas, matching color as closely as possible. Where finish deterioration affects the majority of the wall or area, the whole area should be refinished. The warranty on the newly repainted surfaces will not extend beyond the original warranty period.

Possible Deficiency: Painting required as corollary repair because of other work.

Performance Standard: Necessary repairs required under this warranty should be refinished to match surrounding areas as closely as possible.

Builder Responsibility: Refinish repaired areas as indicated.

Possible Deficiency: Deterioration of varnish or lacquer finishes.

Performance Standard: Natural finishes on interior woodwork should not deteriorate during the first year of ownership. However, varnish type finishes used on the exterior will deteriorate rapidly and are not covered by the warranty.

Builder Responsibility: Retouch affected areas of natural finished interior woodwork, matching the color as closely as possible.

Possible Deficiency: Interior paint quality.

Performance Standard: Interior paint shall be applied in a manner sufficient to visually cover wall, ceiling and trim surfaces where specified.

Builder Responsibility: The builder shall retouch wall, ceiling or trim surfaces where inadequate paint has been applied to cover original surfaces.

10. SPECIALTIES

10200 LOUVERS AND VENTS

Possible Deficiency: Inadequate ventilation of attics and crawl spaces.

Performance Standard: Attic spaces shall have a natural ventilation area equal to (a) 1/150 of floor area or (b) 1/300 of floor area when an accepted vapor barrier is installed on the warm side of the ceiling, or when at least 50% of the required ventilation is provided at least 3 feet above the ceiling. Crawl spaces shall have a natural ventilation area equal to (a) 1/150 of floor area or (b) 1/1500 of the floor area when the surface is covered with an accepted vapor barrier.

Builder Responsibility: The builder shall provide for adequate ventilation.

10300 FIREPLACES

Possible Deficiency: Fireplace or chimney does not draw properly.

Performance Standard: A properly designed [illegible] constructed fireplace and chimney shou[illegible] tion properly. It is norm[illegible] expect [illegible] can cause temporary negative draft situatio. Similar negative draft situations can also be caus by obstructions such as large branches of tre too close to the chimney.

Builder Responsibility: Determine the cause malfunction, and correct as required if the probl is one of design and construction.

11. EQUIPMENT

11900 RESIDENTIAL EQUIPMENT

Possible Deficiency: Kitchen cabinet malfu tions.

Acceptable Tolerance: Kitchen cabinet do drawers and other operating parts should funct properly.

Builder Responsibility: Repair or replace op ating parts as required.

Possible Deficiency: Surface cracks, delami tions and chips in high pressure laminates—Va and Kitchen cabinet countertops.

Performance Standard: Countertops fabric with high pressure laminate coverings should delaminate or have chips or surface cracks.

Builder Responsibility: Repair or replace as condition requires.

15. MECHANICAL

15180 INSULATION (Pipe Covering)

Possible Deficiency: Plumbing pipes freeze

Performance Standard: Drain, waste and ver water pipes should be adequately insulated to vent freezing during normally anticipated weather.

Builder Responsibility: The builder shall co the condition responsible for pipes freezing, repair piping damaged by freezing.

15360 SEPTIC TANK SYSTEMS

Possible Deficiency: Septic system fails to c ate properly.

Performance Standard: Septic system shoul capable of properly handling normal flow of ho hold effluent.

Builder Responsibility: Builder shall take corrective action as required. Builder shall not be responsible for malfunctions which occur through owner negligence or abuse.

15400 PLUMBING

Possible Deficiency: Leakage from any piping.

Performance Standard: No leaks of any kind should exist in any soil, waste, vent or water pipe. Condensation on piping does not constitute leakage, and is not covered.

Builder Responsibility: Builder shall make necessary repairs to eliminate leakage.

Possible Deficiency: Faucet or valve leak.

Performance Standard: No valve or faucet should leak due to defects in material or workmanship. However, leakage caused by worn or defective washers are considered a homeowner maintenance item.

Builder Responsibility: Builder shall repair or replace the leaking faucet or valve unless leakage is due to a defective washer.

Possible Deficiency: Defective plumbing fixtures, appliances or trim fittings.

Performance Standard: Fixtures, appliances or fittings should be judged according to their manufacturing standards.

Builder Responsibility: The builder shall replace any fixture or fitting which is outside of acceptable standards as defined by the manufacturer.

Possible Deficiency: Stopped up sewers, fixtures, and drains.

Performance Standard: Sewers, fixtures and drains should operate properly.

Builder Responsibility: The builder is not responsible for sewers, fixtures and drains which are clogged through the owner's negligence. If a problem occurs, the owner should consult the builder for a proper course of action. Where defective construction is shown to be the cause, the builder shall assume the cost of the repair; where owner negligence is shown to be the cause, the owner shall assume all repair costs.

15500 POWER OR HEAT GENERATION

Possible Deficiency: Inadequate heat.

Performance Standard: Heating system should be capable of producing an inside temperature of 70° F as measured in the center of each room at a height of 5 feet above the floor, under local outdoor winter design conditions as specified in ASHRAE handbook.

Builder Responsibility: Builder shall correct the heating system as required to provide the required temperatures. However, the owner shall be responsible for balancing dampers, registers and other minor adjustments.

15650 REFRIGERATION

Possible Deficiency: Inadequate cooling.

Performance Standard: Where air-conditioning is provided, the cooling system shall be capable of maintaining a temperature of 78° F as measured in the center of each room at a height of 5 feet above the floor, under local outdoor summer design conditions as specified in ASHRAE handbook.

Builder Responsibility: Correct cooling system to meet the above temperature conditions.

15700 LIQUID HEAT TRANSFER
See 15600.

15800 AIR DISTRIBUTION
See 15600 and 15650.

15900 CONTROLS AND INSTRUMENTATION
See 15600 and 15650.

16. ELECTRICAL

16120 CONDUCTORS

Possible Deficiency: Malfunction of electrical switches, fixtures or outlets.

Performance Standard: All switches, fixtures and outlets should operate as intended.

Builder Responsibility: Repair or replace defective wiring, switches, fixtures and outlets.

16140 SWITCHES AND RECEPTACLES
See 16120.

16500 LIGHTING
See 16120.

APPENDIX B

YOUR NEW HOME WARRANTY

TO: ____________________

COMMUNITY: ____________________ LOT NUMBER: ____________________

STREET ADDRESS: ____________________

We want to have satisfied customers It's not only in your best interests, but ours, as well This Home Warranty is your assurance

Like any warranty, this *one* specifies limits for responsibility and conditions under which it is valid or applicable. WE STRONGLY URGE YOU TO READ THIS WARRANTY since it is *the only warranty, express or implied,* that Kaufman and Broad makes to you. *(No employee, salesman* or other agent of Kaufman and Broad is authorized to make any warranty except as herein contained) To assist you, we have tried to avoid fine print or legalistic language

GENERAL ONE-YEAR WARRANTY AND LIMITATIONS

KAUFMAN AND BROAD, INC hereby guarantees THE HOME against defects described below provided that such defects are brought to KAUFMAN AND BROAD's attention, in writing, during the one-year warranty period starting with the date of possession or closing of title of the original purchaser, whichever occurs first, or within such shorter period as may be specified herein (All warranty periods in the paragraphs below shall commence as indicated above)

These guarantees, designed to protect THE HOMEOWNER from the possibility of faulty construction or defective materials, do not cover defects caused by normal wear and tear or by acts or natural disasters, beyond the control of KAUFMAN AND BROAD, nor will KAUFMAN AND BROAD assume *responsibility for* secondary damage caused by any warrantied defect.

Nothing contained in this warranty shall be determined to make KAUFMAN AND BROAD an insurer of the personal property of THE HOMEOWNER or of any third party

The period covered by this warranty can be extended only by a statement in writing signed by an authorized employee of Kaufman and Broad. No other action on the part of Kaufman and Broad or its employees or agents, including any steps taken to correct defects, shall be deemed an extension of such period

KAUFMAN AND BROAD also reserves the right to choose materials and methods used to make repairs

This warranty is applicable to all *items mentioned herein* — if the noted defects are reported in writing before the end of the one-year warranty period or such shorter period as may apply KAUFMAN AND BROAD would like to caution THE HOMEOWNER against having any items covered in this warranty altered by any person or persons other than KAUFMAN AND BROAD, its employees or agents Any items so altered are excluded from warranty coverage, and KAUFMAN AND BROAD will not be liable or responsible for corrective work performed by others nor for its cost.

SERVICE REQUEST ADDRESS

PLEASE READ CAREFULLY THE SCOPE AND TER

STRUCTURAL COMPONENTS

ROOFS

Keeping any gutters and downspouts free of leaves and debris which might cause excessive overflow and keeping all roof areas free of excessive accumulations of snow and ice are among THE HOMEOWNER'S maintenance responsibilities. KAUFMAN AND BROAD guarantees the roof to be free from leaks for a period of one year, except where such defects are caused by acts or natural disasters beyond its control or except where the HOMEOWNER has failed to diligently discharge his maintenance responsibilities. However, this guarantee does not cover damage caused by THE HOMEOWNER or his agents using the roof for any activity, or attaching any superstructure or appurtenance to it which results in damage to the roof.

HEATING

KAUFMAN AND BROAD guarantees proper operation of the heating system, in the original finished room areas, for a period of one year as follows. That the heating system has been installed in accordance with good heating practice and has been designed in accordance with appropriate engineering heat-loss factors to maintain a 70 degree temperature inside the home when outside wind speeds and temperatures are at design conditions established by the American Society of Heating, Refrigerating and Air Conditioning Engineers for the location involved Temperatures are to be measured by readings taken with a verified thermometer in the approximate middle of each room about three feet above the floor. This guarantee does not include the system or any of its parts which become defective through faulty operation, lack of routine maintenance or alteration by THE HOMEOWNER or his agents Such routine maintenance as lubrication and the replacement of filters will be THE HOMEOWNER's responsibility.

AIR CONDITIONING

KAUFMAN AND BROAD guarantees the air conditioning system, if included in the sale of the dwelling, for a period of one year as follows: That the air conditioning system has been installed in accordance with good air conditioning practice and designed in accordance with appropriate engineering heat-gain factors to maintain, in the original finished room areas, at 24 hours continuous operation, a thermostatically controlled environment 15 degrees cooler than the outside temperature; for example, a 78 degree temperature inside with a 93 degree temperature outside. Temperatures are to be read in the approximate middle of each room about three feet above the floor. This guarantee does not include the system or its parts which become defective through faulty operation, lack of routine maintenance or alteration by THE HOMEOWNER or his agents. Normal maintenance functions, such as lubrication and replacement of filters shall be THE HOMEOWNER's responsibility.

PLUMBING

KAUFMAN AND BROAD guarantees the plumbing system against defective workmanship or materials for a period of one year, provided, however, that normal maintenance items such as toilet adjustments and replacement of faucet washers are limited to a 90-day guarantee. Blockage of bathroom fixtures or sewerage lines will be corrected only if it occurs within the first 30 days of the warranty period.

ELECTRICAL SYSTEM

KAUFMAN AND BROAD guarantees the electrical system, excluding light bulbs, against defective workmanship or materials for a period of one year, except where a failure in the system is caused by improper operation, use or alteration caused by THE HOMEOWNER or his agent.

MASONRY

KAUFMAN AND BROAD guarantees all concrete, brick, stone and other masonry against substantial defects for a period of one year.

House slabs, basement floors and walls, garage slabs, walks and other masonry may develop cracks or flaking with the expansion or contraction of cement or concrete due to changes in temperature. KAUFMAN AND BROAD will repair only those cracks which substantially interrupt the plane of the surface or affect its structural value.

1S OF YOUR WARRANTY AS SET FORTH BELOW:

GRADING AND LANDSCAPING
KAUFMAN AND BROAD guarantees for a period of one year that all slopes on THE HOMEOWNER's lot will drain away from his dwelling for an adequate distance (at least ten feet except in case of unusual terrain). These guarantees do not apply to damage resulting from alterations of grades by persons other than KAUFMAN AND BROAD, or its agents, or resulting from failure of THE HOMEOWNER to assume normal responsibilities for the maintenance of his landscaping and grounds. Minor erosion of the yard areas can be expected with a new home and is the responsibility of THE HOMEOWNER to correct.

Any trees, shrubs, sod or seeding provided are guaranteed to live for one growing season after occupancy, provided regular watering, fertilization and pruning are provided for by THE HOMEOWNER.

DRIVEWAYS
KAUFMAN AND BROAD guarantees for a period of one year the driveway against major settlement. Of course minor indentations, tire marks, oil spots or other surface imperfections inherent to paved surfaces are not included, and THE HOMEOWNER should remember that residential driveways are not designed to handle heavy trucks. Damage resulting from unusually heavy loads will not be corrected by KAUFMAN AND BROAD. THE HOMEOWNER should follow the HOMEOWNER's MANUAL recommendation for proper maintenance of driveways. (See page 13.)

WATER INFILTRATION

HOUSE BUILT WITH SLAB ON GRADE
KAUFMAN AND BROAD guarantees the underslab air ducts (if any) against penetration by free water for a period of one year. This guarantee does not cover condensation, backing up of sewers, flash floods, hurricanes, leaks through windows which are not properly maintained or other events beyond the control of KAUFMAN AND BROAD. **This guarantee shall not apply if a person other than KAUFMAN AND BROAD or its agent has altered or disturbed the air ducts, or the finished grade adjacent to the house, or elsewhere on the lot, if the result is to change the drainage pattern of the ground adjacent to or near the house.**

HOUSE WITH BASEMENT OR CRAWL SPACE
KAUFMAN AND BROAD guarantees for a period of one year basements and crawl spaces against penetration of free flowing water (as distinguished from the dampness which is characteristic of most home basements and crawl spaces). This guarantee does not cover condensation, backing up of sewers, flash floods, hurricanes, leaks through windows which are not properly maintained, or other events beyond the control of KAUFMAN AND BROAD. **This guarantee shall not apply if a person other than KAUFMAN AND BROAD or its agent has altered the finished grade adjacent to the house, or elsewhere on the lot, if the result is to change the drainage pattern adjacent to or near the house.** In areas where sump pumps are installed by KAUFMAN AND BROAD because of high water tables or other conditions which cause water infiltration to be inevitable, KAUFMAN AND BROAD's guarantee is limited to the proper functioning of the sump pump for a period of one year. **It is necessary, however, that the homeowner keep sump pump and sump pump pit clean. Our warranty will not be effective in the event of defects due to dirt or debris.**

EXCESSIVE WARPAGE
KAUFMAN AND BROAD guarantees against excessive warpage of structural members, doors, counter-tops, vanities, as well as delamination of plywood for a period of one year. "Excessive" warpage shall mean more than ⅜ inch in the case of doors; more than ⅜ inch in a 48-inch span in the case of vanities and countertops; and more than ¼ inch in the case of structural members. New exterior doors may temporarily warp during periods of rapid temperature change and later return to shape. Therefore, such warpage is excluded under this guarantee.

Continued on page 4

GENERAL

Structural components not specifically covered above are warranted by KAUFMAN AND BROAD for a period of one year as defined above against faulty construction and/or defective materials.

ASSIGNMENT OF MANUFACTURERS' WARRANTIES

KAUFMAN AND BROAD assigns to THE HOMEOWNER its interest in any manufacturers' warranties for mechanical equipment, appliances and other manufactured items furnished with the house, and KAUFMAN AND BROAD does not, itself, warrant these items

NON-WARRANTABLE ITEMS

KAUFMAN AND BROAD delivers your new home cleaned in accordance with normal construction standards. But, in fairness, we cannot take it upon ourselves to make good on move-in damage or other damage caused by persons other than KAUFMAN AND BROAD, its employees or agents.

And, we would like to clear up an issue that causes many new HOMEOWNERS needless alarm and irritation: A new home goes through a settling process. While settling, your home may develop small cracks, visible nailheads, expansion or contraction of materials in walls, floors, ceilings, doors, windows and other locations which is to be expected. While we realize these items might cause momentary concern, they are easily remedied when THE HOMEOWNER does his first repainting. KAUFMAN AND BROAD is not responsible for correcting normal settlement deviations nor for making a perfect color match when touch-up repairs are made on painted surfaces.

Stained woods used in cabinets, paneling, siding, doors and wood trim all have variations in wood grain and color These are inherent characteristics which cannot be fully controlled and are therefore excluded from the guarantee.

The following defects will be corrected by KAUFMAN AND BROAD only (1) if they are significant, (2) if they resulted from the acts of KAUFMAN AND BROAD or its agents, and (3) if they are noted in writing at the time of the Walk Through Inspection.

(a) Defects in the appearance of interior and exterior finished surfaces
(b) Chipping of porcelain, tile, vitreous china and counter and vanity tops
(c) Torn or defective screens and/or storm windows
(d) Broken glass and mirrors
(e) Defects in siding, trim or lighting fixtures
(f) Defects in appliance finishes
(g) Loose screws, nuts and bolts
(h) Missing items

Any such defect not noted in writing at the time of the Walk Through Inspection will be the responsibility of THE HOMEOWNER to correct

WARRANTY TRANSFERABLE TO SUBSEQUENT PURCHASER

If the original HOMEOWNER sells the premises before the warranty period has expired, the subsequent purchaser shall succeed to the original HOMEOWNER's remaining rights and time under this warranty.

KAUFMAN AND BROAD, INC. makes no warranties other than those described above. KAUFMAN AND BROAD's obligations under this warranty are limited solely to making the necessary repairs in a workmanlike manner.

294-972 O - 80 - 19

YOUR
NEW HOME
WARRANTY
FROM

KAUFMAN AND BROAD, INC.

ACKNOWLEDGMENT

The undersigned on this ______ day of __________ 19____ acknowledge receipt of the NEW HOME WARRANTY given by KAUFMAN AND BROAD, INC. in the community of __________

______________________________.

I acknowledge that I have read the attached warranty and understand its contents. I agree to notify KAUFMAN AND BROAD in writing when requesting service. I further understand that there will be no reimbursement from KAUFMAN AND BROAD for work privately contracted for by me without written permission from KAUFMAN AND BROAD, in advance. Finally, I understand that Kaufman and Broad does not extend to me any warranty, either express or implied, other than those contained in the attached NEW HOME WARRANTY and I acknowledge that except for the attached NEW HOME WARRANTY no employee or agent of Kaufman and Broad has made any representation or guarantee on which I am entitled to rely.

____
SIGNED

____
SIGNED

APPENDIX C

State of ______________________)
) SS.
County/City of ________________)
)

AFFIDAVIT

____
(First Name(s)) (Last Name)

being duly sworn, depose(s) and says:

1. I (we) am (are) the original purchaser(s) and purchased the home at the following address _______________

______________________________, ______________________,
(Street address) (Town)

______________________________, ______________________
(State) (Name of subdivision)

from Kaufman and Broad, Inc. or one of its companies, and the date of settlement/closing was ______________________,
(enter date you took title)
and have continously held title to this home from that date to the date of this affidavit.

2. My (our) request is not for a repair that Kaufman and Broad, Inc. or any of its companies, agents, employees, or subcontractors previously fully completed.

3. I (we) have not signed a release or received payment or other remedial action or made any other settlement with Kaufman and Broad or any of its companies in connection with the request for repair now made.

4. I (we) hereby agree, in consideration of Kaufman and Broad's offer to make repairs under certain conditions, that I (we) shall assign to Kaufman and Broad the proceeds of any insurance I (we) may have that covers the defect described in paragraph 5 of this affidavit, to the extent of the cost to Kaufman and Broad of any repair or replacement it may make pursuant to this request.

5. I (we) request Kaufman and Broad to make the following repair(s) which I (we) believe to be a "major construction defect" under the terms of their letter of notification:

(Use additional sheets if necessary. Describe in detail the nature of the defect. <u>Your description should include</u>: (1) the nature of the damage; (2) the load-bearing part of the home affected; and (3) the manner in which the damage vitally affects or is imminently likely to produce a vital effect on the use of the home for residential purposes).

All of the above information is true and correct to the best of my (our) knowledge.

Subscribed and sworn to me before this ______ day of
________________, 197__.

____
Signature

____
Notary Public

____
Signature

Page 1

APPENDIX D

State of ______________________)
) SS.
County/City of ________________)
)

AFFIDAVIT

____
(First Name(s)) (Last Name)

being duly sworn, depose(s) and says:

1. I (we) am (are) the original purchaser(s) and purchased the home at the following address ______________

_________________________, ____________________________,
(Street address) (Town)

___________________, ____________________________ from
(State) (Name of subdivision)

Kaufman and Broad, Inc. or one of its companies, and the date of settlement/closing was ________________________,
(enter date of you took title)
and have continously held title to this home from that date to the date of this affidavit.

2. My (our) request is not for a repair that Kaufman and Broad, Inc. or any of its companies, agents, employees or subcontractors previously fully completed.

3. I (we) have not signed a release or received payment or other remedial action or made any other settlement with Kaufman and Broad or any of its companies in connection with the request for repair now made.

4. I (we) hereby agree, in consideration of Kaufman and Broad's offer to make repairs under certain conditions that I (we) shall assign to Kaufman and Broad the proceeds of insurance I (we) may have that covers the defect(s) described in paragraph 5 of this affidavit, to the extent of the cost to Kaufman and Broad of any repair or replacement it may make pursuant to this request.

5. I (we) request Kaufman and Broad to make the following repair(s) under the terms of their letter of notification:

(Use additional sheets if necessary. Describe in detail the nature of the defect(s). If you are requesting repair to a <u>major construction defect</u> then, in addition your description should include: (1) the nature of the damage; (2) the load-bearing part of the home affected; and (3) the manner in which the damage vitally affects or is imminently likely to produce a vital effect on the use of the home for residential purposes.)

All of the above information is true and correct to the best of my (our) knowledge.

Subscribed and sworn to
before me this _____ day
of __________, 197__.

____
Signature

____
Notary Public

____
Signature

(SEAL)

APPENDIX E

LETTER OF NOTIFICATION

Dear Kaufman and Broad Homeowner:

This letter is to notify you that you may be entitled to have certain repairs made to your home at no cost to you.

Kaufman and Broad recently agreed with the Federal Trade Commission to extend to its previous customers the same warranty protection K&B now gives to new customers. Therefore, if you bought a new home directly from us or any of our companies between January 1, 1972 and (ending two years prior to the day immediately preceding the effective date of the order) we will repair any "major construction defect" in your home without charge to you.

What is a "major construction defect"? You'll find the definition and the exclusions on the attached pages 3 and 4 of this letter. This definition and the exclusions were drawn up by the National Association of Home Builders for their nationwide "HOW" warranty program. We use this same definition and exclusions in the warranty we give our new customers. Study pages 3 and 4 of this letter carefully. Then check your home, inside and outside, for the major construction defects you think we should repair. Maybe get advice from someone who knows about such things.

Please notice that a "major construction defect" covers the major structural elements of your home, such as the foundation, load-bearing walls, and the roof structure. It does not cover minor items due to normal wear and tear, or cracking due to normal settlement and shrinkage, or such other similar matters.

To file a claim for repair to a "major construction defect," do this:

Fill in the blank spaces in the attached affidavit. Sign it before a notary public. Then mail it <u>certified mail</u>, <u>return receipt requested</u>, to (<u>name and address of respondents' designated office</u>).

Be sure to mail it by ________________. <u>IT MUST BE POSTMARKED 50 DAYS FROM THE DATE OF THIS LETTER</u>. If you miss the deadline, we can refuse to do the free repairs.

If your request is on time and justified, we'll let you know within 45 days when we'll make the repairs. Or, if your request is not justified, we'll let you know why. If there's a dispute we can't settle within 40 days from the date the dispute arises, we can go to arbitration.

If the defect is a common element in a condominium, have the affidavit signed by the Board of Directors but <u>not</u> by any board members who represent the builder.

This is part of our continued effort to make you, the Kaufman and Broad home buyer, a comfortable and satisfied homeowner.

Sincerely,

KAUFMAN AND BROAD, INC

DEFINITION OF "MAJOR CONSTRUCTION DEFECT

A "major construction defect" is actual damage to the load-bearing portion of the home (including damage due to subsidence, expansion or lateral movement of soil from causes other than flood or earthquake) which affects its load-bearing function and which vitally affects (or is imminently likely to produce a vital effect on) the use of the home for residential purposes.

EXCLUSIONS

You are not entitled to make a claim for the following:

1. Defects in plumbing, electrical, heating and cooling systems.

2. Defects in appliances, fixtures, and items of equipment.

3. Defects in outbuildings (except that outbuildings which contain the plumbing, electrical, heating, or cooling systems serving the home are covered), swimming pools and other recreational facilities; driveways; walkways; patios; boundary walls; retaining walls which are not necessary for the home's structural stability; fences; landscaping (including sodding, seeding, shrubs, trees and plantings); offsite improvements; or any other improvements not a part of the home itself.

4. Bodily injury, damage to personal property, or real property which is not part of the home which was included in the purchase price.

5. Any damage to the extent it is caused or made worse by:

   - Negligence, improper maintenance or improper operation by anyone other than Kaufman and Broad or any of its companies, or its employees, agents or subcontractors; or

   - Failure of anyone other than Kaufman and Broad or any of its companies or its employees, agents or subcontractors to comply with the warranty requirements of manufacturers of appliances, equipment or fixtures; or

   - Changes of the grading of the ground by anyone other than Kaufman and Broad, Inc. or any of its companies, or its employees, agents or subcontractors.

6. Any defect in, or caused by, materials or work supplied by anyone other than Kaufman and Broad or any of its companies or its employees, agents, or subcontractors.

7. Normal wear and tear or normal deterioration.

8. Accidental loss or damage from causes such as, but not limited to: fire, explosion, smoke, water escape, changes which are not reasonably forseeable in the level of the underground water table, glass breakage, wind storm, hail, lightning, falling trees, aircraft, vehicles, flood and earthquake. HOWEVER, SOIL MOVEMENT FROM CAUSES OTHER THAN FLOOD OR EARTHQUAKE IS NOT EXCLUDED.

9. Insect damage.

10. Any loss or damage which arises while the home is being used primarily for non-residential purposes.

11. Any defect which does not result in actual loss or damage.

APPENDIX F

LETTER OF NOTIFICATION

Dear Kaufman and Broad Homeowner:

This letter is to notify you that you may be entitled to have certain repairs made to your home at no cost to you.

Kaufman and Broad recently agreed with the Federal Trade Commission to extend to its previous customers the same warranty protection K&B now gives to new customers. Therefore, if you bought a new home directly from us or any of our companies since (2 years prior to and including the day immediately preceding the effective date of the order) we will repair major construction defects, and certain defects in the plumbing, electrical, heating and cooling systems in your home without charge to you.

You'll find the definitions of these types of defects, and the exclusions, on pages 3 and 4 of this letter and also in the attached "Approved Standards." This definition, the exclusions, and the "Approved Standards" were drawn up by the National Association of Home Builders for their nationwide "HOW" warranty program. We use the same definition, exclusions, and approved standards in the warranty we give our new customers.

Study pages 3 and 4 of this letter carefully, and also the attached "Approved Standards." Then check your home, inside and outside, for the defects you think we should repair. Maybe get advice from someone who knows about such things.

Please notice that a "major construction defect" covers the major structual elements of your home, such as the foundation, load-bearing walls, and the roof structure. It does not cover minor items due to normal wear and tear, or cracking due to normal settlement and shrinkage, or such other similar matters. Also, the "Approved Standards" explain in detail what a defect is, and also explains what the builder is required to do to correct the defect.

To file a claim for repairs, do this:

Fill in the blank spaces in the attached affidavit. Sign it before a notary public. Then mail it certified mail, return receipt requested, to (name and address of respondents' designated office).

Be sure to mail it by ____________________. IT MUST BE POSTMARKED 50 DAYS FROM THE DATE OF THIS LETTER. If you miss the deadline, we can refuse to do the free repairs.

If your request is on time and justified, we'll let you know within 45 days when we'll make the repairs. Or, if your request is not justified, we'll let you know why. If there's a dispute we can't settle within 40 days from the date the dispute arises, we can go the arbitration.

If the defect is a common element in condominium, have the affidavit signed by the Board of Directors but not by any board members who represent the builder.

This is part of our continued effort to make you, the Kaufman and Broad home buyer, a comfortable and satisfied homeowner.

Sincerely,

KAUFMAN AND BROAD, INC

DEFINITIONS

MAJOR CONSTRUCTION DEFECT

A "major construction defect" is actual damage to the load-bearing portion of the home (including damage due to subsidence, expansion or lateral movement of soil from causes other than flood or earthquake) which affects its load-bearing function and which vitally affects (or is imminently likely to produce a vital effect on) the use of the home for residential purposes.

PLUMBING, ELECTRICAL, HEATING AND COOLING SYSTEMS
SEE ATTACHED APPROVED STANDARDS

also

SEE EXCLUSION #1 BELOW

EXCLUSIONS

You are not entitled to make a claim for the following:

1. Defects in appliances, fixtures, and items of equipment.

2. Defects in outbuildings (except that outbuildings which contain the plumbing, electrical, heating or cooling systems serving the home are covered); swimming pools and other recreational facilities; driveways; walkways; patios; boundary walls; retaining walls which are not necessary for the home's structural stability; fences; landscaping (including sodding, seeding, shrubs, trees and planting); offsite improvements; or any other improvements not a part of the home itself.

3. Bodily injury, damage to personal property, or real property which is not part of the home which was included in the purchase price.

4. Any damage to the extent it is caused or made worse by:

   - Negligence, improper maintenance or improper operation by anyone other than Kaufman and Broad or any of its companies, or its employees, agents or subcontractors; or

   - Failure of anyone other than Kaufman and Broad or any of its companies, or its employees, agents or subcontractors to comply with the warranty requirements of manufacturers of appliances, equipment or fixtures; or

Changes of the grading of the ground by anyone other than Kaufman and Broad, Inc. or any of its companies, or its employees, agents or subcontractors.

5. Any defect in, or caused by, materials or work supplied by anyone other than Kaufman and Broad or any of its companies or its employees, agents, or subcontractors.

6. Normal wear and tear or normal deterioration.

7. Accidental loss or damage from causes such as, but not limited to: fire, explosion, smoke, water escape, changes which are not reasonably forseeable in the level of the undeground water table, glass breakage, wind storm, hail, lightning, falling trees, aircraft, vehicles, flood and earthquake. HOWEVER, SOIL MOVEMENT FROM CAUSES OTHER THAN EARTHQUAKE IS NOT EXCLUDED.

8. Insect damage.

9. Any loss or damage which arises while the home is being used primarily for non-residential purposes.

10. Any defect which does not result in actual loss or damage.

In the Matter of

CPC INTERNATIONAL INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND CLAYTON ACTS

Docket C-2955. Complaint, Feb. 22, 1979 — Decision, Feb. 22, 1979

This order, among other things, requires an Englewood Cliffs, N.J. food products manufacturer and its wholly-owned Danville, Ill. subsidiary, Peterson/Puritan, Inc., to divest, within 18 months from the date of the order, the aerosol packaging facility in Atlanta, Ga. acquired from the Capitol Packaging Company. Additionally, the order prohibits respondents from competing with the facility for two years following divestiture, and bars them from acquiring any contract aerosol packaging concern without prior Commission approval for a five-year period.

Appearances

For the Commission: *Robert W. Doyle, Jr.*

For the respondents: *Robert F. Finkle, Mayer, Brown & Platt,* Chicago, Ill.

Complaint

The Federal Trade Commission having reason to believe that the above-named respondents, each subject to the jurisdiction of the Commission, have acquired the assets, as hereinafter described, of a corporation subject to the jurisdiction of the Commission, in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint pursuant to Section 11 of the Clayton Act (15 U.S.C. 21), and Section 5(b) of the Federal Trade Commission Act (15 U.S.C. 45(b)) stating its charges as follows:

I. DEFINITIONS

Paragraph 1. For the purposes of this complaint, the following definitions apply:

(a) An "aerosol product" is any personal care product, household product, coating or finish, food product, insect spray, automotive product, or animal product that is packaged in a pressurized aerosol container together with a liquefied or compressed gas propellant necessary to expel the product from the container.

(b) A "contract aerosol packager" is any firm that packages aerosol products, pursuant to contract or otherwise, for one or more firms to which it is unaffiliated.

II. RESPONDENTS

A. CPC International Inc.

PAR. 2. Respondent CPC International Inc. (hereinafter "CPC") is a corporation chartered and operating under the laws of the State of Delaware, with a principal place of business located at the International Plaza, Englewood Cliffs, New Jersey.

PAR. 3. CPC manufactures and sells to industrial users in the United States products derived principally from the refining of corn, and also manufactures and sells domestically a variety of consumer products, mainly food products.

PAR. 4. In 1976, CPC worldwide had revenues of almost $2.7 billion, assets of almost $1.5 billion, and net income in excess of $120 million. In 1976, CPC ranked 79th on Fortune Magazine's list of the 500 largest industrial corporations.

PAR. 5. CPC achieved entry into contract aerosol packaging in 1966 through the acquisition of Peterson Filling and Packaging Co. (hereinafter "Peterson").

PAR. 6. In 1968, Peterson acquired the Puritan Aerosol Corporation (hereinafter "Puritan"), a corporation chartered and operating under the laws of the Commonwealth of Massachusetts, with a principal place of business located at Martin St., Cumberland, Rhode Island.

PAR. 7. Prior to its acquisition by Peterson, Puritan was a leading contract packager of aerosol products, with aerosol packaging facilities in Cumberland, Rhode Island and Santa Fe Springs, California.

PAR. 8. On or about October 13, 1971, Peterson merged Puritan into Peterson to form Peterson/Puritan, Inc.

PAR. 9. At all times relevant hereto, CPC sold and shipped its products and services throughout the United States, was engaged in commerce within the meaning of the Clayton Act, as amended, and was engaged in or affected commerce within the meaning of the Federal Trade Commission Act, as amended.

B. Peterson/Puritan, Inc.

PAR. 10. Respondent Peterson/Puritan, Inc. (hereinafter "P/P"), a wholly-owned domestic subsidiary corporation of respondent CPC, is chartered and operates under the laws of the State of Delaware, with a principal place of business located at Hegeler Lane, Danville, Illinois.

PAR. 11. P/P is the leading contract aerosol packager in the United States, with aerosol packaging facilities located in Danville, Illinois; Cumberland, Rhode Island; Santa Fe Springs, California; Atlanta, Georgia; and Momence, Illinois.

PAR. 12. P/P packaged 218 million units of aerosol products in 1976, accounting for almost 22 percent of the aerosol units produced by contract aerosol packagers in that year.

PAR. 13. At all times relevant hereto, P/P sold and shipped its products and services throughout the United States, was engaged in commerce within the meaning of the Clayton Act, as amended, and was engaged in or affected commerce within the meaning of the Federal Trade Commission Act, as amended.

III. THE ACQUISITION

PAR. 14. On or about April 1, 1977, P/P purchased for approximately $2.5 million substantially all of the aerosol packaging assets of Capitol Packaging Co. (hereinafter "Capitol"), a corporation chartered and operating under the laws of the State of Illinois as a wholly-owned subsidiary of the Alberto-Culver Co.

PAR. 15. Prior to the aforementioned acquisition, Capitol was a leading contract aerosol packager, having packaged 62 million units of aerosol products in 1976, and accounting for approximately 6 percent of the aerosol units produced by contract aerosol packagers in that year.

PAR. 16. At all times relevant hereto, Capitol sold and shipped its products and services throughout the United States, and was engaged in commerce within the meaning of the Clayton Act, as amended.

IV. TRADE AND COMMERCE

PAR. 17. The relevant geographic market is the United States as a whole.

PAR. 18. The relevant line of commerce is the packaging of aerosol products by contract aerosol packagers (hereinafter "the relevant line of commerce").

PAR. 19. Approximately 2.0 billion aerosol units were packaged in the United States in 1976. Of these, approximately 1.0 billion units were packaged by contract aerosol packagers.

PAR. 20. Concentration in the relevant line of commerce is high.

PAR. 21. Barriers to entry into the relevant line of commerce are substantial.

PAR. 22. Prior to the subject acquisition, as hereinbefore described, P/P and Capitol were substantial actual competitors in the relevant line of commerce.

V. EFFECTS OF THE ACQUISITION

PAR. 23. The effect of the aforesaid acquisition may be substantially to lessen competition or to tend to create a monopoly in the relevant line of commerce throughout the United States in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45) in the following ways, among others:

(a) Substantial actual potential competition in the relevant line of commerce between P/P and Capitol, and other firms in the relevant line of commerce has been eliminated;

(b) Concentration in the relevant line of commerce has been and/or may be increased to the detriment of actual and potential competition;

(c) The substantial likelihood of lessening concentration in the relevant line of commerce has been diminished and/or eliminated;

(d) The position of P/P in the relevant line of commerce has been and/or may be further strengthened and entrenched; and

(e) The ability of P/P's competitors to compete in the relevant line of commerce has been and/or may be substantially diminished.

VI. THE VIOLATIONS CHARGED

PAR. 24. The aforesaid acquisition constitutes a violation of Section 7 of the Clayton Act, as amended, and Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of an acquisition by the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with a violation of the Federal Trade Commission Act and the Clayton Act; and

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Acts, and that a complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34(b) of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent CPC International Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at International Plaza, Englewood Cliffs, New Jersey.

Respondent Peterson/Puritan, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at Hegeler Lane, Danville, Illinois.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

Order

For the purposes of this order, the following definitions shall apply:

(a) "Respondents" refers to CPC International Inc., a corporation; Peterson/Puritan, Inc., a corporation; and said corporations' subsidiaries, affiliates, successors and assigns.

(b) "Person" means any individual, corporation, partnership, association, firm, or other business or legal entity.

(c) "Aerosol product" means any personal care product, household product, coating or finish, food product, insect spray, automotive product, or animal product that is packaged in a pressurized aerosol container together with a liquefied or compressed gas propellant necessary to expel the product from the container.

(d) "Aerosol packaging facilities" means any plant, machinery, or equipment used to package aerosol products in the United States, and also includes the whole or any part of the stock, share capital, or

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any interest in any person engaged in the packaging of aerosol products in the United States.

I

It is ordered, That, within eighteen (18) months after the date of this order and subject to the prior approval of the Federal Trade Commission, respondents shall divest the aerosol packaging facility in Atlanta, Georgia (hereinafter "the Atlanta facility") acquired from the Capitol Packaging Company, together with any and all additions and improvements thereto, as a viable business concern.

II

It is further ordered, That, for a period of two (2) years after the Atlanta facility is divested, respondents shall not package aerosol products in the U.S. for:

(a) any persons (other than the Alberto-Culver Co.) who, as of March 30, 1977, were customers of the Atlanta facility but were not aerosol packaging customers of respondents;

(b) any persons who, between March 31, 1977 and March 31, 1978, were aerosol packaging customers of respondents at only the Atlanta facility; and

(c) any persons who first became aerosol packaging customers of respondents after March 31, 1978 and for whom respondents packaged a greater number of aerosol units at the Atlanta facility between March 31, 1978 and the date of divestiture than at all of their other facilities combined.

III

It is further ordered, That, for a period ending two (2) years after the Atlanta facility is divested, respondents shall neither directly nor indirectly solicit any persons who have been customers of the Atlanta facility at any time since March 31, 1977 to divert any of their aerosol packaging requirements from the Atlanta facility to one or more of respondents' other facilities.

IV

It is further ordered, That the Atlanta facility shall not be divested to any person who, as of the date of divestiture, is an officer, director, employee or agent of respondents, or who directly or indirectly owns or controls more than one (1) percent of the outstanding stock of respondents.

V

It is further ordered, That, pending divestiture of the Atlanta facility, respondents shall neither make nor permit any deterioration in said facility, other than normal wear and tear, which may impair its market value on the date of this order.

VI

It is further ordered, That, for a period of five (5) years from the date of this order, respondents shall neither directly nor indirectly acquire, without the prior approval of the Federal Trade Commission, any aerosol packaging facilities from any person engaged in the business of packaging aerosol products for one or more persons that are unaffiliated with the owner of said facilities.

VII

It is further ordered, That, within sixty (60) days after the date of this order and every sixty (60) days thereafter until the divestiture ordered by Paragraph I hereof is effected, respondents shall submit to the Federal Trade Commission a detailed written report setting forth the manner and form in which they have complied with this order. All such compliance reports shall include, among other things, that are from time to time required, a summary of all discussions and negotiations with any persons who are potential owners of the assets to be divested, the identity of all such persons, copies of all communications to and from such persons, and all internal memoranda, reports and recommendations concerning divestiture.

VIII

It is further ordered, That respondents shall notify the Federal Trade Commission at least thirty (30) days prior to any proposed change in their corporate structures, such as dissolution, assignment or sale resulting in the emergence of successor corporations, the creation or dissolution of subsidiaries, or any other change in said respondents which may affect compliance obligations arising out of this order.

IN THE MATTER OF

THE KROGER COMPANY

Docket 9102. Interlocutory Order, Feb. 26, 1979

ORDER DENYING MOTION FOR RECONSIDERATION AND DENYING MOTION TO DISQUALIFY ADMINISTRATIVE LAW JUDGE

Respondent has moved for reconsideration of our recent order affirming the administrative law judge's ("ALJ") denial of respondent's motion for discovery of certain documents in the files of the Commission. Respondent has also moved to disqualify the ALJ, Montgomery K. Hyun, on the ground that because he had access to many of these same documents during his prior employment as attorney-advisor to former Chairman Engman, his continued participation creates an actual or apparent impropriety. Respondent perceives an impropriety because "it appears that [Judge Hyun] may decide the case or have his reaction to evidence preconditioned by ex-record material and discussion on pertinent issues arising from his activities engaged in before becoming an administrative law judge." Affidavit of Stuart J. Land at 6. Judge Hyun declined to disqualify himself and certified respondent's motion to the Commission, pursuant to Section 3.42(g) of our Rules of Practice.

The Issue of Disqualification

This case concerns, *inter alia,* allegations that respondent, which owns a chain of supermarkets, made comparative price claims about the relative costs to consumers of its products, which claims were based upon methodologically unsound price surveys. Judge Hyun accepted an assignment to this matter only on the basis, which he has expressly reaffirmed, that he had no recollection of advising former Chairman Engman on, or otherwise dealing with, any matter pertaining to respondent or to retail food advertising generally during his tenure as an attorney-advisor. Respondent has not suggested that the contrary is true. Thus, the only question with which we are presented here is whether disqualification of an administrative law judge is mandated where in his prior employment he had access to, but does not recall reviewing, materials which, respondent contends, might influence his reaction to record evidence and thus lead him to render a biased decision.

The Nature of the Claim

Judge Hyun resigned from the Commission in September 1973; the preliminary investigation underlying the instant complaint was not opened until December 1975, and the complaint itself was not issued until July 1977. Accordingly, respondent cannot and does not allege that the documents to which Judge Hyun had access bear specifically on the allegations against it. Instead, respondent avers that the Commission documents concern and would reflect upon the ease or difficulty of designing and implementing a methodologically valid retail food price survey generally. Collectively, respondent claims, such documents would tend to be exculpatory in nature.[1] But, it is apparent, respondent could only benefit from any preconditioning of the mind of Judge Hyun resulting from his exposure to allegedly exculpatory information. To assert this disqualification claim, therefore, respondent avers that at the time of Judge Hyun's resignation from the Commission, the exculpatory nature of the document may not yet have become evident, because the Commission's staff had not yet comprehended or reported the difficulties of devising a sound methodology. Thus, it is alleged, during his seven-month service as an attorney-advisor, Judge Hyun would have had access only to documents which might not prove to be exculpatory after all, and that he therefore may be "preconditioned," if one presumes he actually read or discussed the documents, to react other than positively to respondent's defense asserting the unreasonable difficulty of conducting a methodologically valid survey.

Disposition of the Motion for Disqualification

Because we do not perceive an appearance of impropriety, we decline either to reverse our earlier determination concerning document production[2] or to order the disqualification of the ALJ. Even if all the allegations contained in the moving affidavit are taken as true, respondent would still fall short. As we have previously stated, an ALJ should be disqualified only upon an adequate showing of bias or prejudgment. Mere access to internal Commission documents tangentially relevant to a proceeding cannot be grounds for his dismissal, notwithstanding that such access has served, under our Rules of Practice, as grounds for denial of clearance to a former Commission employee who wished to appear as counsel for respondent in this litigation. *See* letter of November 16,

[1] On this basis, respondent has sought, unsuccessfully, to have all such documents, including those which the ALJ has ruled are exempt from disclosure by reason of privilege, produced and admitted into evidence in this litigation. Judge Hyun has, of course, ordered production to respondent of all relevant non-privileged factual materials, including exculpatory information, in the possession of the Commission.

[2] As noted at the outset, we recently affirmed Judge Hyun's denial of respondent's motion for production of otherwise privileged Commission documents. Respondent has asked us, in connection with the motion for disqualification of Judge Hyun, to reconsider this determination, so that it might "lay bare facts which would either confirm or dispel the appearance of impropriety that now exists." Motion for Reconsideration at 2.

1978 to S. Mark Tuller, Esq. As we have noted previously, our clearance rules address issues wholly distinct from those pertinent to disqualification of a law judge.[3]

The two instances cited by respondent in which disqualification was ordered by a Court of Appeals because an individual acting in an adjudicative capacity had gained knowledge of relevant facts while serving in a prior, non-judicial capacity, differ materially from this case and do not support respondent's contention that Judge Hyun must be disqualified.

In *American Cyanamid Co.* v. *FTC,* 363 F.2d 757 (6th Cir. 1966), it was proved that a member of the Commission, in his role as Chief Counsel to the Subcommittee on Antitrust and Monopoly of the Senate Judiciary Committee, had personally investigated the same facts and issues concerning the same parties named as respondents in an administrative proceeding, prior to adjudicating that proceeding in his subsequent role as Chairman of the Commission. The decision plainly is not based on the Commissioner's access to pertinent information in his role as Chief Counsel but rather upon his extensive personal conduct, which the court held to be sufficient to unseat the presumption of impartiality. Indeed, the Court of Appeals specifically stated that the Commissioner's service, standing alone, as counsel to the subcommittee that was undertaking the investigation, would not necessarily require his disqualification. 363 F.2d at 768.

In *United States* v. *Amerine,* 411 F.2d 1130 (6th Cir. 1969), a criminal case, the court ordered the disqualification of a district court judge who had tried and sentenced a defendant against whom the original complaint had been issued during the period of the judge's prior service as United States Attorney. There are critical distinctions between *Amerine* and the instant case, even beyond the undeniable asymmetry of the criminal and civil laws. First, the complaint in this case was not issued until four years after Judge Hyun's resignation from the Commission, a salient distinction which eliminates any need for disqualification. *See United States* v. *Wilson,* 426 F.2d 268 (6th Cir. 1970); *Barry* v. *United States,* 528 F.2d 1094 (7th Cir.), *cert. den.,* 429 U.S. 826 (1976); *United States* v. *Kelly,* 556

[3] In the clearance context, the Commission's primary concern is with the perception that a former employee may have an advantage in representing a client by reason of having had access to nonpublic information, and as a matter of policy the Commission has decided to base its determinations on an essentially objective standard—likelihood of access and opportunity to be exposed to such information—rather than to rely solely upon the subjective standard of actual exposure. In the present context, however, respondent's claim of disqualification rests largely upon the supposed effects of actual exposure to certain information, and the Commission has concluded in any event that, under its precedents, even actual exposure would not be disqualifying, *see infra.* Alternative Ground for Disposition of Motion to Disqualify, there being no comparable problem of a former Commission employee using for private purposes information acquired while a Commission employee.

F.2d 257 (5th Cir. 1977), *cert. den.,* 434 U.S. 1017 (1978). Second, Mr. Hyun's role as attorney-advisor to a Commissioner is hardly akin to that of a United States Attorney, who exercises supervisory responsibility and at least nominally initiates charges and issues complaints. Finally, *Amerine* is of limited utility in any event, since the opinion rested solely upon a statutory construction of the former version of 28 U.S.C. 455, under which the judge was deemed to have been "of counsel" to the government by dint of his former role as United States Attorney.

Finally, respondent urges upon us the current version of 28 U.S.C. 455(b) (1976), as amended in 1974, which mandates the disqualification of a federal judge who has "personal knowledge of disputed evidentiary facts concerning the proceeding" or who "participated as . . . adviser . . . concerning the proceeding" while "in governmental employment." The proposed application of the statute to the facts at hand cannot be sustained. First, the statute on its face does not apply to administrative law judges,[4] and respondent's argument that the courts have so extended the statute, Application for Review of ALJ's Order of January 15, 1979 at 12, lacks support. There is considerable authority, apart from the application of maxims of construction, which suggests that Section 455 does not apply to agency adjudicators, whose potential disqualification is to be tested instead against the standard set out in the Administrative Procedure Act ("APA"). *See* 5 U.S.C. 556(b) (1976); *Securities and Exchange Comm'n* v. *R. A. Holman & Co.,* 323 F.2d 284, 287 (D.C. Cir.), *cert. den.,* 375 U.S. 943 (1963); *Converse* v. *Udall,* 262 F.Supp. 583 (D. Ore. 1966), *aff'd,* 399 F.2d 616 (9th Cir. 1968), *cert. den.,* 393 U.S. 1025 (1969). The APA gives appropriate recognition to the varied functions performed by agencies which federal judges would not be expected to perform. Where Congress has not explicitly subjected agencies to the same strictures applicable to federal courts, it would be inappropriate to subject an agency's actions to the same standards. *See generally Vermont Yankee Nuclear Power Corp* v. *NRDC,* 435 U.S. 519 (1978); *FTC* v. *Flotill Prods., Inc.,* 389 U.S. 179, 183–85 (1967); *United States* v. *Morton Salt Co.,* 338 U.S. 632, 641–42 (1950).

Second, assuming *arguendo* that the statute does apply, it does not require Judge Hyun's disqualification. The judge has specifically denied having any "personal knowledge" whatever concerning this proceeding, and he has specifically denied that he "participated as an advisor" concerning this proceeding. The authorities are also clear that under Section 455, a necessary precondition to disqualifi-

[4] Only justices, judges, magistrates and referees in bankruptcy are expressly covered.

cation is that the proceeding in question have been initiated during the judge's prior tenure in a non-judicial capacity, a hurdle which respondent plainly fails to surmount here. *See United States* v. *Kelly, supra; Barry* v. *United States, supra.*

In the absence of some evidence extrinsic to the discovery in this case, which suggests that Judge Hyun's stated recollections are mistaken, we see no basis for disqualification or even for further inquiry. There is nothing to suggest that the judge will decide the case on the basis of anything other than the record evidence. Respondent has failed utterly to demonstrate that Judge Hyun has "a bent of mind that may prevent or impede impartiality of judgment." *Berger* v. *United States,* 255 U.S. 22, 33–34 (1921).

Alternative Ground for Disposition of Motion to Disqualify

As an alternative and independent ground for affirmance, the Commission is of the view that Commission rule and precedent, as well as the Administrative Procedure Act, dispose of respondent's arguments.

For example, *Grolier, Inc.,* 87 F.T.C. 179, 180 (1976), *aff'd* 91 F.T.C. 486 (1978), contradicts respondent's position. There, the Commission held that even an ALJ's prior participation as an attorney-advisor in "provid[ing] advice during the precomplaint stage of an investigation" would not alone be sufficient to order his disqualification on the grounds of alleged improper commingling of functions, possible bias, or possible exposure to information not later admitted into evidence. In the instant case, of course, Judge Hyun has stated that he has no present recollection of participating in this matter, and we have no reason to question his statements. *Cf. National Nutritional Foods Ass'n* v. *FDA,* 491 F.2d 1141, 1144–46 (2d Cir.), *cert. den.,* 419 U.S. 874 (1974); *Hercules* v. *EPA,* No. 77–1248, slip op. at 59–62 (D.C. Cir. Nov. 3, 1978). Judge Hyun's conduct thus falls well within the ambit of activity protected by *Grolier.*

Neither is the relief sought by respondent required by the APA. Section 7, 5 U.S.C. 556, of course, mandates impartiality, but does not aid respondent, because respondent has failed completely to overcome the strong presumption of honesty and fairmindedness attributed to agency adjudicators. *See Withrow* v. *Larkin,* 421 U.S. 35, 47, 55 (1975). Indeed, under respondent's argument a Commissioner who had access to the same information as Judge Hyun could not then preside at the reception of evidence, a result clearly inconsistent with the APA.

Disposition of the Motion for Reconsideration

Respondent's motion for reconsideration must be denied. Absent some extrinsic evidence of bias or prejudgment by the ALJ, respondent is not entitled to discovery of otherwise privileged documents to which it has sought and been denied access already in this proceeding. *Cf. United States* v. *Litton Industries, Inc.*, 462 F.2d 14 (9th Cir. 1972); *R. A. Holman & Co.* v. *S.E.C.*, 366 F.2d 446 (2d Cir. 1966), *cert. den.*, 389 U.S. 991 (1967). The naked conclusory allegation of bias, resting upon a hypothetical preconditioning of the mind of the ALJ resulting from his possible exposure to documents which he does not recall, does not state a need sufficient to overcome a proper assertion of privilege. Accordingly,

It is ordered, That respondent's motion for reconsideration of the Order Affirming Order Ruling on Respondent's Motion for Production of Documents be, and it hereby is, denied. And,

It is further ordered, That respondent's motion for disqualification of the administrative law judge be, and it hereby is, denied.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

LOUISIANA-PACIFIC CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND CLAYTON ACTS

Docket C-2956. Complaint, Feb. 27, 1979 — Decision, Feb. 27, 1979

This consent order, among other things, requires a Portland, Ore. firm engaged in harvesting and converting timber into various wood products, including medium density fiberboard (MDF) and particleboard, to divest, within two years to a Commission-approved buyer, the Rocklin MDF plant, which firm acquired through its merger with the Fiberboard Corporation; and offer the new buyer the opportunity to purchase from the firm, for five years, a limited amount of the raw materials necessary to manufacture MDF. Additionally, the order prohibits the firm, for ten years, from acquiring, without prior agency approval, any entity engaged in the manufacture of particleboard or MDF.

Appearances

For the Commission: *James Egan.*

For the respondent: *William E. Willis, Sullivan & Cromwell,* New York City.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondent, subject to the jurisdiction of the Commission, has entered into a merger agreement which, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, that said agreement constitutes a violation of Section 5 of the Federal Trade Commission Act, as amended, and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, pursuant to Section 11 of the Clayton Act, 15 U.S.C. 21, and Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. 4(b), stating its charges in the following Count I.

The Federal Trade Commission, having further reason to believe that the above-named respondent also has violated and is violating Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, through the acquisition of the stock and/or assets of various corporations, and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, pursuant to Section 11 of the Clayton Act, 15 U.S.C. 21, and Section 5(b), of the Federal

Trade Commission Act, 15 U.S.C. 45(b), stating its charges in the following Count II.

COUNT I

I. Louisiana Pacific Corporation

PARAGRAPH 1. Louisiana Pacific Corporation (L-P) is a corporation organized under the laws of the State of Delaware with its principal place of business located at 1300 S.W. Fifth Ave., Portland, Oregon.

PAR. 2. L-P is a diversified, integrated forest products company. It grows and harvests timber which it then converts to various wood products, including lumber, plywood, particleboard, veneer, pulp and wood chips. In 1977 L-P had total shipments of particleboard in excess of $56 million and total sales of lumber in excess of $330 million.

PAR. 3. In 1977 L-P had net sales in excess of $794 million and net income in excess of $60 million.

II. Fibreboard Corporation

PAR. 4. Fibreboard Corporation (F-B) is a corporation organized under the laws of the State of Delaware with its principal place of business located at 55 Francisco St., San Francisco, California.

PAR. 5. F-B is a diversified, integrated forest products company. It grows and harvests timber, which it then converts to various wood products, including lumber, plywood, medium density fiberboard (MDF), pulp and wood chips. It is also involved in the manufacture and sale of container products and insulation. F–B's total shipments of MDF in 1977 exceeded $10 million and its total sales of forest products exceeded $51 million.

PAR. 6. In 1977 F-B had net sales in excess of $227 million and net income in excess of $1.2 million.

III. Jurisdiction

PAR. 7. At all times relevant herein L-P and F-B have been engaged in the manufacture and sale of various products, including those products relevant to this complaint, in interstate commerce and are engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. 12, and each is a corporation whose business is in or affecting commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

IV. The Merger Agreement

PAR. 8. On March 22, 1978 L-P and F-B entered into a merger agreement which provides, inter alia, for the merger of F-B into L-P. The merger agreement further provides that, upon consummation of the merger, F-B will become a wholly-owned subsidiary of L-P. The value of the transaction is in excess of $56 million.

V. Trade and Commerce

PAR. 9. The relevant markets are:

a. The manufacture in the United States of particleboard and MDF, and the sale thereof.

b. The manufacture in the Western Region of the United States of particleboard and MDF, and the sale thereof.

c. The manufacture in the Pacific Coast Region of the United States of particleboard and MDF, and the sale thereof.

PAR. 10. The Western Region of the United States as used herein includes the States of Arizona, California, Colorado, Idaho, Montana, New Mexico, Oregon, Nevada, Utah, Washington and Wyoming. Of these states particleboard and/or MDF is actually produced only in the States of California, Idaho, Montana, New Mexico, Oregon and Washington. The Pacific Coast Region of the United States as used herein includes the States of California, Oregon and Washington.

PAR. 11. Concentration in each of the relevant markets enumerated in Paragraph 9 of this complaint is already high and increasing.

PAR. 12. Barriers to entry into each of the relevant markets enumerated in Paragraph 9 of this complaint are already high and increasing.

VI. Actual Competition

PAR. 13. L-P and F-B are now and have been since at least 1975 actual competitors of each other in each of the relevant markets enumerated in Paragraph 9 of this complaint, and actual competitors of others engaged in each of the relevant markets enumerated in Paragraph 9 of this complaint.

PAR. 14. L-P is the largest manufacturer, by capacity, of particleboard/MDF in the United States, accounting, in 1978, for approximately 12.4 percent of all capacity in that market. In 1978 F-B had approximately 1.3 percent of the total capacity in that market. In terms of actual production, L-P was the second largest producer in 1977 accounting for approximately 11.1 percent of all particleboard/MDF produced in the United States. In that same year F-B accounted for approximately 1.3 percent of total production in that market.

PAR. 15. L-P is the largest manufacturer, by capacity, of particleboard/MDF in the Western Region of the United States, accounting, in 1978, for approximately 14.5 percent of all capacity in that market. In 1978 F-B was ranked twelfth in that market in terms of capacity with approximately 2.9 percent of the total. In terms of actual production, L-P was the third largest producer in 1977 accounting for approximately 14.1 percent of all particleboard/MDF produced in the Western Region of the United States. In the same year F-B ranked thirteenth in terms of production accounting for 2.9 percent of the market.

PAR. 16. L-P is the third largest manufacturer, by capacity, of particleboard in the Pacific Coast Region of the United States accounting in 1978, for approximately 11.4 percent of all capacity in that market. In 1978 F-B was ranked eleventh in that market in terms of capacity with approximately 3.3 percent of the total. In terms of actual production, L-P was the fourth largest producer in 1977 accounting for approximately 10.0 percent of all particleboard/MDF produced in the Pacific Coast Region of the United States. In the same year F-B ranked twelfth in terms of production accounting for approximately 3.5 percent of the market.

VII. Effects; Violations Charged

PAR. 17. The effects of the proposed acquisition may be to substantially lessen competition or tend to create a monopoly in the relevant markets enumerated in Paragraph 9 of this complaint in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, in the following ways, among others:

(a) actual competition between L-P, F-B and others in the manufacture and sale of particleboard/MDF will be eliminated; and

(b) concentration in the manufacture and sale of particleboard/MDF will be increased and the possibilities for eventual deconcentration may be diminished.

COUNT II

VIII. Louisiana-Pacific Corporation

PAR. 18. The allegations as set forth in Paragraphs 1 through 3, inclusive of Count I are hereby incorporated by reference and made a part of Count II as if rewritten herein.

IX. Evans Products Company

PAR. 19. Evans Products Company is a corporation organized under the State of Delaware with its principal place of business located at 1121 S.W. Salmon St., Portland, Oregon.

PAR. 20. Evans Products Company is engaged in the manufacturing, marketing and retailing of building materials including lumber, plywood, plywood specialities, and precut homes, and the manufacturing, marketing and leasing of transportation and industrial equipment. In 1975, its last full year of particleboard production, Evans Products Company had particleboard shipments in excess of $9 million.

X. Georgia-Pacific Corporation

PAR. 21. Georgia-Pacific Corporation ("G-P") is a corporation organized under the laws of the State of Delaware with its principal place of business located at 900 S.W. Fifth Ave., Portland, Oregon.

PAR. 22. G-P is a diversified integrated forest products company. It grows and harvests timber which it then converts to various wood products, including lumber, plywood, particleboard and wood chips. In 1975 G-P had particleboard shipments in excess of $31 million.

XI. Jurisdiction

PAR. 23. The allegations as set forth in Paragraph 7 of Count I which relate to L-P are hereby incorporated by reference and made part of Count II as if fully rewritten herein.

PAR. 24. At all times relevant herein Evans Products and G-P have been engaged in the manufacture and sale of various products, including those products relevant to this complaint, in interstate commerce and are engaged in commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

XII. The Acquisitions

PAR. 25. On April 2, 1976, L-P purchased from Evans Products Company a particleboard plant in Missoula, Montana for $11,798,000 (including plant and related assets).

PAR. 26. On August 30, 1976, L-P leased a particleboard plant from G-P at Ukiah, California ("Ukiah") for a period of five years at an average annual payment of $480,000. L-P has the option to purchase the plant at the end of 3 years.

XIII. Trade and Commerce

PAR. 27. The relevant markets are:

a. The manufacture in the United States of particleboard and MDF, and the sale thereof.

b. The manufacture in the Western United States of particleboard and MDF, and the sale thereof.

c. The manufacture in the Pacific Coast Region of the United States of particleboard and MDF, and the sale thereof.

PAR. 28. The allegations as set forth in Paragraph 10 of Count I are hereby incorporated by reference and made a part of Count II as if rewritten herein.

PAR. 29. At the time of the acquisitions by L-P of the Missoula particleboard plant and the Ukiah particleboard plant, the manufacture of particleboard/MDF and the sale thereof in the relevant markets as enumerated in Paragraph 27 of this complaint was highly concentrated and increasing.

PAR. 30. Barriers to entry into the manufacture and sale of particleboard/MDF are substantial and are increasing.

XIV. Actual Competition

PAR. 31. At the time of the acquisitions, L-P and Evans Products Company were and had been since at least 1975, actual competitors of each other in the relevant markets as enumerated in Paragraph 27, subparts a. and b. of this complaint and actual competitors of others engaged in the relevant markets as enumerated in Paragraph 27, subparts a and b, of this complaint.

PAR. 32. At the time of the acquisitions, L-P and G-P were and had been since 1975, actual competitors of each other in the relevant markets as enumerated in Paragraph 27 of this complaint, and actual competitors of others engaged in the relevant markets as enumerated in Paragraph 27 of this complaint.

PAR. 33. In 1975, the year preceeding the acquisitions L-P accounted for approximately 5.3 percent of all particleboard/MDF production in the United States; 3.9 percent of all particleboard/MDF production in the Western Region of the United States and 4.6 percent of all particleboard/MDF production in the Pacific Coast Region of the United States. In that same year, G-P's Ukiah plant accounted for 1.6 percent of all particleboard production in the

United States; 3.3 percent of all particleboard/MDF production in the Western Region of the United States and 3.9 percent of all particleboard/MDF production in the Pacific Coast Region of the United States. In that same year, Evans Products Company accounted for 2.9 percent of all particleboard/MDF production in the United States and 6.1 percent of all particleboard/MDF production in the Western Region of the United States.

XV. Effects, Violations Charged

PAR. 34. The effects of the acquisitions may be to substantially lessen competition or tend to create a monopoly in the relevant markets enumerated in Paragraph 27 of this complaint in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, **and** Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, in the following ways, among others:

(a) actual competition between L-P, G-P, Evans Products Company and others in the manufacture and sale of particleboard/MDF has been eliminated; and

(b) concentration in the manufacture and sale of particleboard/MDF has been increased and the possibilities for eventual deconcentration have been diminished.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with a violation of the Federal Trade Commission Act and the Clayton Act; and

The respondent and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all jursidictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having considered the matter and having determined that it had reason to believe that the respondent has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following findings and enters the following order:

1. Respondent Louisiana-Pacific Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal place of business at 1300 S.W. Fifth Ave., Portland, Oregon.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent and the proceeding is in the public interest.

ORDER

For the purpose of this order, the following definitions shall apply:

(a) "Particleboard" is a flat panel product consisting of particles of wood bonded together with a synthetic resin or other suitable bonding system by a process in which the interparticle bond is created by the bonding systems, as further described in Commercial Standard CS236-66, published by the United States Department of Commerce, National Bureau of Standards, and as reported under the Standard Industrial Classification Manual No. 24921.

(b) "Medium density fiberboard" is a dry-formed panel product manufactured from lignocellulosic fibers, combined with a synthetic resin or other suitable binder, by the application of heat and pressure in which the interfiber bond is substantially created by the added binder, as further described in the standard published by the National Particleboard Association, N.P.A. 4-73, and as reported under the Standard Industrial Classification Manual No. 24997.

(c) The "Rocklin MDF plant" consists of land, plant, property, equipment and machinery presently owned and operated by Fibreboard Corporation for the manufacture of medium density fiberboard at Rocklin, California, to be acquired by respondent as a result of its merger with Fibreboard Corporation, including all additions, replacements and improvements thereto hereafter made by respondent.

I

It is ordered, That respondent, its officers, directors, agents, representatives and employees shall, absolutely and in good faith

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divest, within two (2) years from the date this order becomes final, subject to the prior approval of the Federal Trade Commission, all rights, title and interest in and to the Rocklin MDF plant acquired by respondent as a result of its merger with Fibreboard Corporation.

II

It is further ordered, That in connection with any divestiture of the said Rocklin MDF plant, respondent will offer to any prospective acquirer the right to enter into a contract to buy from respondent (or its subsidiary Fibreboard Corporation) for use in said plant at Rocklin, California wood residue raw materials of the type currently being supplied by Fibreboard Corporation's internal operations to said plant, which contract will include provisions substantially as follows:

(a) the contract will continue for a minimum of five (5) years;
(b) prices will be market prices existing in the the area during the contract term for similar wood residue raw materials; and
(c) quantities to be sold in each year will equal at least the total quantity of said wood residue raw materials heretofore supplied to said plant from Fibreboard Corporation's own internal operations in the year 1977, or which will be supplied in the year 1978, or double the total quantity of said materials so supplied in the first six months of 1978, whichever is greatest.

III

It is further ordered, That none of the assets and properties required to be divested by respondent pursuant to Paragraph I above, shall be divested directly or indirectly to anyone who is, at the time of divestiture, an officer, director, employee, or agent of, or under the control, direction or influence of respondent, or who owns or controls more than one percent of the capital stock of respondent.

IV

It is further ordered, That respondent shall cease and desist for a period of ten (10) years from the date this order becomes final from acquiring, directly or indirectly, through subsidiaries or otherwise, without the prior approval of the Commission, (1) the whole or any part of the stock or share capital or any concern, corporate or noncorporate, engaged at the time of acquisition in any State of the United States in the manufacture of (a) particleboard, or (b) medium density fiberboard, or (2) a manufacturing plant or facility engaged at the time of acquisition in any State of the United States in the manufacture of (a) particleboard, or (b) medium density fiberboard. Any exercise hereafter by respondent of its option to purchase the Ukiah, California particleboard plant presently operated by respondent pursuant to a lease shall not be prohibited by this paragraph.

V

It is further ordered, That respondent shall within one (1) year from the date this order becomes final, and every sixty (60) days after one (1) year until respondent has fully complied with the provisions of Paragraphs I and II of this order, submit in writing to the Federal Trade Commission a verified report setting forth in detail the manner and form in which respondent intends to comply or has complied with this order. All compliance reports shall include a summary of contacts or negotiations with anyone for the specified assets, the identity of all such persons, and copies of all written communications to and from such persons.

VI

It is further ordered, That respondent notify the Federal Trade Commission at least thirty (30) days prior to any proposed change in the corporate respondent which may affect compliance obligations arising out of the order, such as dissolution, assignment or sale resulting in the emergence of a successor corporation or the creation or dissolution of subsidiaries.

IN THE MATTER OF

LANCASTER COLONY CORPORATION, ET AL.

DISMISSAL ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND CLAYTON ACTS

Docket 9119. Complaint, Oct. 25, 1978 — Dismissal Order, March 6, 1979

This order dismisses the complaint against two manufacturers of machine-made glassware alleging violations of Section 7 of the Clayton Act, and Section 5 of the Federal Trade Commission Act. The Commission, in dismissing the complaint, held that under the unique circumstances presented in this case, further proceedings in the matter are not in the public interest.

Appearances

For the Commission: *Edward T. Colbert* and *William D. Mitchell.*

For the respondents: *Richard Murphy* and *Fred A. Summer, Dunbar, Kiezel & Murphy,* Columbus, Ohio, *Edward Wolf, J.B. Rather* and *R.W. Davis, White & Case,* New York City and *John W. Barnum, White & Case,* Washington, D.C.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondents, each subject to the jurisdiction of the Commission, have entered into an acquisition agreement which, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, that said agreement already constitutes a violation of Section 5 of the Federal Trade Commission Act, as amended, and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, pursuant to Section 11 of the Clayton Act, 15 U.S.C. 21, and Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. 45(b), stating its charges as follows:

I

Definition

PARAGRAPH 1. For the purpose of this complaint, the following definition shall apply: "Machine-made glassware" means all moderately-priced soda-lime glass beverageware, tableware, food preparation glassware, and novelty and ornamental glassware items produced by machine.

II

Federal Paper Board Company, Inc.

PAR. 2. Federal Paper Board Company, Inc. (Federal Paper) is a corporation organized and existing under the laws of the State of New York, with a principal place of business at 75 Chestnut Ridge Road, Montvale, New Jersey.

PAR. 3. Federal Paper through its unincorporated Federal Glass Company division (Federal Glass) produces machine-made glassware and sells said machine-made glassware throughout the United States.

PAR. 4. In its fiscal year ended December 31, 1977, Federal Paper had net sales of approximately $397,000,000, and net income of approximately $13,800,000; Federal Glass had net sales of approximately $48,000,000 and income before allocation for taxes and corporate overhead of approximately $910,000.

PAR. 5. Federal Glass is the third largest manufacturer of machine-made glassware in the United States.

PAR. 6. Federal Glass, until 1978, was for many years a member of the American Glassware Association, which is a trade association made up of the major domestic manufacturers of machine-made glassware.

III

Lancaster Colony Corporation

PAR. 7. Lancaster Colony Corporation (Lancaster Colony) is a corporation organized and existing under the laws of the State of Delaware, with a principal place of business at 37 West Broad St., Columbus, Ohio.

PAR. 8. Lancaster Colony, through its subsidiary Indiana Glass Company, an Indiana corporation, produces machine-made glassware, and sells said machine-made glassware throughout the United States. Lancaster Colony also produces machine-made glassware through its subsidiary Lancaster Glass Corporation, an Ohio corporation, and sells said machine-made glassware throughout the United States.

PAR. 9. In its fiscal year ended June 30, 1978, Lancaster Colony had sales of approximately $237,000,000, and net income of approximately $23,300,000. Lancaster Colony had sales of machine-made glassware of approximately $35,500,000.

PAR. 10. Indiana Glass Company is the fourth largest manufacturer of machine-made glassware in the United States.

PAR. 11. Indiana Glass Company, until 1978, was for many years a member of the American Glassware Association, which is a trade association made up of the major domestic manufacturers of machine-made glassware.

IV

Jurisdiction

PAR. 12. At all times relevant herein Federal Paper and Lancaster Colony have been engaged in the manufacture and sale of machine-made glassware in interstate commerce and are engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. 12, and each is a corporation whose business is in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

V

The Acquisition Agreement

PAR. 13. On or about April 1978 Federal Paper and Lancaster Colony agreed in principle to the acquisition by Lancaster Colony of all Federal Glass assets of Federal Paper. The proposed purchase agreement provides, *inter alia,* for the sale of the Federal Glass assets of Federal Paper in exchange for approximately $42,000,000. A letter of intent was executed by Lancaster Colony on August 29, 1978.

VI

Trade and Commerce

PAR. 14. Relevant lines of commerce are the manufacture and sale of machine-made glassware and submarkets thereof.

PAR. 15. A relevant section of the country or geographic market is the entire United States.

PAR. 16. The United States machine-made glassware market is highly concentrated with the combined market share of the four largest manufacturers estimated to be approximately 74 percent.

PAR. 17. Barriers to entry into the manufacture of machine-made glassware and submarket thereof are substantial.

VII

Actual Competition

PAR. 18. Federal Paper and Lancaster Colony are and have been for many years actual competitors in the manufacture and sale of machine-made glassware and submarkets thereof, and actual competitors of others engaged in the manufacture and sale of machine-made glassware and submarkets thereof throughout the United States.

VIII

Effects

PAR. 19. The effect of the proposed acquisition may be to substantially lessen competition or to tend to create a monopoly in the relevant market in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, or Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, in the following ways, among others:

(a) actual competition between Federal Paper and Lancaster Colony in the manufacture and sale of machine-made glassware and submarkets thereof will be eliminated;

(b) actual competition between competitors generally in the manufacture and sale of machine-made glassware and submarkets thereof may be lessened;

(c) Federal Paper will be eliminated as an actual substantial independent competitor in the manufacture and sale of machine-made glassware and submarkets thereof;

(d) concentration in the manufacture and sale of machine-made glassware and submarkets thereof will be increased and possibilities for eventual deconcentration may be diminished;

(e) mergers or acquisitions between other machine-made glassware manufacturers may be encouraged, thus causing a further substantial lessening of competition and tendency toward monopoly in the relevant markets.

IX

Violations Charged

PAR. 20. The proposed acquisition by Lancaster Colony of the Federal Glass assets of Federal Paper (if consummated), the proposed Purchase Agreement between Lancaster Colony and Federal Paper (if executed), and the agreement in principle between

Lancaster Colony and Federal Paper, constitute violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and are or would be unfair acts, practices or methods of competition in violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

Order Granting Complaint Counsel's Motion To Withdraw from Adjudication and To Dismiss the Complaint

The administrative law judge (ALJ) has certified to the Commission the motion of respondent Federal Paper Board Company, Inc. (Federal) to terminate this proceeding by an order prohibiting the sale of any of the assets of its Federal Glass Division (Division) to respondent Lancaster Colony Corporation (Lancaster). Also certified to the Commission is complaint counsel's motion to withdraw the case from adjudication and to dismiss the complaint. The ALJ recommends that the Commission accept Federal's motion and deny that of complaint counsel.

The Division has been closed since January 31, 1979, when Federal announced the shutdown of its plant, alleging continuing operating losses. However, Federal has refused to provide complaint counsel with financial and other relevant information in support of its "failing company" defense. In their papers, complaint counsel note that the withdrawal of the Wheaton Glass Co. and the Eastcliff Corporation from negotiations to purchase the Division have exhausted all feasible alternatives to liquidation of the Division or sale to Lancaster. Complaint counsel recognize the possibility that some other purchaser might exist but suggest that the slight chance of identifying another party which will expeditiously return the plant to normal operation is not worth the gamble of approximately 1500 jobs at stake. Counsel further point out that liquidation of the Division could result in the loss of its customers to the two largest firms in this industry, Anchor Hocking Corporation and the Libbey Division of Owens-Illinois.

Under these rather unique circumstances, and in the exercise of our discretion, we conclude that further proceedings in this matter are not in the public interest. Accordingly,

It is ordered, That the complaint in this matter is hereby dismissed.

IN THE MATTER OF

CHILDREN'S ADVERTISING

TRR No. 215-60. Interlocutory Order, March 7, 1979

ORDER MODIFYING SCHEDULE

Effective March 9, 1979, the Commission will be temporarily reduced to four members, of whom two are not presently participating in the instant proceeding. Whether or not two Commissioners might properly exercise certain decisionmaking authority under these circumstances, the Commission believes that, if at all reasonably possible, it is in the public interest that Commission decisions of significance with respect to this proceeding be taken with the participation of no fewer than three Commissioners. At the same time, certain phases of most Magnuson-Moss rulemaking proceedings, including this one, typically involve little or no intervention by the Commission because of the wide latitude to conduct hearings vested in the presiding officer. It would be productive of considerable delay, and manifestly not in the public interest, were such phases of a matter to be suspended merely because of the desire of the Commission that decisions to be made at some unspecified time in the future be made with the participation of no fewer than three members.

In light of the foregoing, the Commission can perceive no reason why the presently ongoing "legislative" hearings in this matter, which are subject to the direction of the presiding officer, ought not proceed as scheduled. Nor does any reason appear why interested parties may not thereafter propose issues for designation, or why the presiding officer may not subsequently recommend designation of such issues.[1] However, it is the present intention of the Commission that it will not designate such issues as contemplated by the Initial Notice of Rulemaking, 43 F.R. 17967, 17971 (April 27, 1978) until it may do so pursuant to a vote in which at least three members of the Commission participate. To achieve these results the following order is issued:

It is ordered, That following completion of the Washington, D.C. "legislative" hearing in this matter, persons wishing to do so must submit to the presiding officer on or before April 30, 1979, or by such other time as the presiding officer may in his sole discretion establish (1) proposed disputed issues of fact that are material and

[1] The Initial Notice of Proposed Rulemaking, 43 F.R. 17967, *et seq.* (April 27, 1978), makes no express reference to the role of the presiding officer in the designation process. It was the Commission's intention that the presiding officer should make a recommendation to the Commission as to what issues, if any, should be designated.

necessary to resolve at a disputed issues hearing, (2) requests to cross-examine at a disputed issues hearing witnesses who appeared at the "legislative" hearings, and (3) requests to present oral rebuttal at a disputed issues hearing.

It is further ordered, That following receipt of the submissions ordered above, the presiding officer shall make a recommendation to the Commission identifying disputed issues of fact, if any, that are material and necessary to resolve at a disputed issues hearing.

It is further ordered, That subsequent proceedings in this matter shall be had at such time as the Commission shall hereafter order.

Chairman Pertschuk and Commissioner Pitofsky did not participate.

In the Matter of

TRW, INC., ET AL.

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND CLAYTON ACTS

Docket 9084. Complaint, June 17, 1976 — Final Order, March 8, 1979

This order, among other things, requires a Cleveland, Ohio manufacturer and seller of electronic point-of-sale credit authorization equipment to cease having on its board of directors any individual who is simultaneously serving as a director of Addressograph-Multigraph Corp., or any other competitive business entity. The order also prohibits Horace A. Shepard from simultaneously serving as a director of TRW, Inc. and any other competing company.

Appearances

For the Commission: *John M. Mendenhall* and *Paul P. Eyre.*

For the respondents: *Richard W. Pogue, Robert H. Rawson* and *Brent L. Henry, Jones, Day, Reavis & Pogue,* Cleveland, Ohio and *Joseph D. McGarth,* Baker Heights, Ohio.

Complaint

The Federal Trade Commission, having reason to believe that the above-named respondents have been and are in violation of the provisions of Section 8 of the Clayton Act, as amended, and Section 5(a)(1) of the Federal Trade Commission Act, as amended, and that a proceeding in respect thereof would be in the public interest, issues this complaint, stating its charges as follows:

Paragraph 1. Respondent TRW, Inc., (hereinafter TRW), is an Ohio corporation and maintains its principal office at 23555 Euclid Ave., Cleveland, Ohio. TRW has capital, surplus, and undivided profits aggregating more than One Million Dollars ($1,000,000). TRW is engaged in commerce, as "commerce" is defined in Section 1 of the Clayton Act, and is engaged in or its business affects commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act.

Par. 2. Respondent Addressograph-Multigraph Corporation (hereinafter Addressograph) is a Delaware corporation and maintains its principal office at 20600 Chagrin Boulevard, Shaker Heights, Ohio. Addressograph has capital, surplus, and undivided profits aggregating more than One Million Dollars ($1,000,000). Addressograph is engaged in commerce, as "commerce" is defined in Section 1 of the Clayton Act, and is engaged in or its business affects commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act.

PAR. 3. Respondent Horace A. Shepard is an individual. His business address is the same as that of TRW.

PAR. 4. On or about April 29, 1969, respondent Horace A. Shepard was elected director and chief executive officer of TRW and has served in such capacities with TRW from on or about April 29, 1969, until the present. On or about November 4, 1971, respondent Horace A. Shepard was elected director of Addressograph and has served in such capacity with Addressograph from on or about November 4, 1971, until on or about November 6, 1975.

PAR. 5. During all or part of the period January 1, 1973 through and including November 6, 1975, the business of TRW and Addressograph included, but was not limited to, the manufacture, sale and distribution in commerce of point-of-sale credit authorization equipment and teller-operated bank transaction equipment, and other such equipment used for credit validation, check cashing validation, recording of deposits and withdrawals from financial institutions, and inventory record keeping.

PAR. 6. By the nature of their business as hereinabove described and location of operations with respect thereto, Addressograph and TRW were competitors, concurrent with respondent Horace A. Shepard's membership on the Boards of Directors of TRW and Addressograph, during part or all of the period January 1, 1973 through and including November 6, 1975, so that the elimination of competition by agreement between them would constitute a violation of the antitrust laws.

PAR. 7. The simultaneous membership of respondent Horace A. Shepard on the Boards of Directors of respondents TRW and Addressograph constitutes a violation of Section 8 of the Clayton Act, 15 U.S.C. 19, and Section 5(a)(1) of the Federal Trade Commission Act, 15 U.S.C. 45.

INITIAL DECISION BY JOSEPH P. DUFRESNE, ADMINISTRATIVE LAW JUDGE

DECEMBER 22, 1977

PRELIMINARY STATEMENT

In a complaint dated June 17, 1976, the Commission charged that respondents TRW, Inc., Addressograph-Multigraph Corporation (A-M) and Horace A. Shepard, had violated Section 8 of the Clayton Act,

as amended, (15 U.S.C. 19) and Section 5(a)(1) of the Federal Trade Commission Act, as amended, (15 U.S.C. 45(a)(1)). [2]
Section 8, in pertinent part, reads as follows:

> . . . no person at the same time shall be a director in any two or more corporations, any one of which has capital surplus, and undivided profits aggregating more than $1,000,000, engaged in whole or in part in commerce, . . . if such corporations are or shall have been theretofore, by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws. . . .

Section 5(a)(1) provides:

> Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful.

The gravamen of the charges was that the simultaneous membership of Mr. Shepard on the boards of directors of TRW and A-M from January 1, 1973, through November 6, 1975 (hereinafter referred to as the "critical period"), constituted a violation of the Clayton and FTC Acts (Complaint, ¶¶ 4 and 7). This, because during the critical period the business of TRW and A-M ". . . included, but was not limited to, the manufacture, sale and distribution in commerce of point-of-sale credit authorization equipment and teller-operated bank transaction equipment, and other such equipment used for credit validation, check cashing validation, recording of deposits and withdrawals from financial institutions and inventory record keeping" (Complaint, ¶ 5).

The result alleged was that, since TRW and A-M were competitors due to the nature of their business and location of operations, coupled with Mr. Shepard's simultaneous membership on the boards of each, elimination by agreement between them of competition between TRW and A-M would constitute a violation of the antitrust laws (Complaint, ¶ 6). [3]

In their answers, in pertinent part, TRW and Mr. Shepard:

1. Denied having violated Section 8 of the Clayton Act, Section 5 of the FTC Act and denied a proceeding, as alleged in the introductory paragraph of the complaint, was in the public interest. They also denied, for want of knowledge sufficient to form a belief, the allegations regarding A-M. (Answers, ¶¶ 1 and 3);
2. Admitted (1) TRW's capital, surplus and individual profits aggregate more than $1,000,000, (2) that it is engaged in commerce or that its business affects commerce as "commerce" is defined in the FTC Act, and (3) that Mr. Shepard is an individual whose address is the same as that of TRW. (Answers, ¶¶ 2 and 3);
3. Averred that Mr. Shepard became a director of TRW on March

26, 1957, chief executive officer of TRW on December 22, 1969, continued in these positions and that on or about March 20, 1971, became and continued to serve as a director of A-M until November 6, 1975. (Answers, ¶ 4);

4. Admitted that between January 1, 1973, and December 6, 1975, TRW's business included the manufacture, and distribution in commerce, of products falling in the generic categories of equipment described above. They denied knowledge as to A-M's products and denied that TRW and A-M were competitors, so that the elimination of competition by agreement between them would constitute a violation of the antitrust laws, during the critical period. They also denied that Section 8 and Section 5 had been violated. [4]

The following affirmative defenses were asserted:

1. The complaint did not state a claim upon which relief could be granted (Answers, ¶ 7);

2. Mr. Shepard had decided prior to August 8, 1975 (when he first learned of the Commission's investigation - RX 54A; Solganik, Tr. 1961-62), to leave the Board of Directors of A-M, did so on November 6, 1975, and the issues raised by the complaint were moot (Answers, ¶ 8);

3. The relevant period was between October 1973, when A-M first sold an AMCAT and November 7, 1974, the date of Mr. Shepard's last election to the Board of A-M (Answers, ¶ 9) during which period A-M and TRW were not competitors (Answers, ¶ 10) and that any alleged competition between them was *de minimis* (Answers, ¶ 11);

4. TRW and Mr. Shepard were denied their rights of due process, denied equal protection of the laws and subjected to abuse of process (Answers, ¶¶ 12 and 13);

5. Section 5 of the FTC Act should not be applied to an interlocking directorate which is not violative of Section 8 of the Clayton Act (Answers, ¶ 14);

6. Section 8 of the Clayton Act does not apply to corporations (Answer of TRW, ¶ 15);

7. The proceedings were not in the public interest (Answers, ¶¶ 16 and 15, respectively); and

8. There is neither a reasonable expectation the alleged wrong vould be repeated nor a need for issuance of an order (Answers, ¶¶ 7 and 16, respectively). [5]

Prehearing conferences were held on November 4, 1976 by ALJ aniel Hanscom, to whom the case was assigned initially, and by me ı May 9 and 25, 1977, and on June 27, 1977. Motions for summary cision were made both by complaint counsel and TRW. These her have been denied or are denied by this decision.

In a negotiated order described in a "Decision and Order" dated August 11, 1977, [90 F.T.C. 144] the charges as to A-M were resolved. In the order, A-M admitted all the jurisdictional facts alleged in the complaint and stipulated that consent to the order did not constitute an admission that the law had been violated.

The Consent Order: (1) prohibits A-M from having interlocking directorates with competitors if the elimination of competition by agreement between them would constitute a violation of the antitrust laws; (2) requires preparation of a list by each A-M director of the products, names and addresses of other corporations on whose board the director sits or to which he/she has been nominated; (3) requires A-M to review prior to each election of directors and to retain for each member of its board of directors and nominees, a descriptive list of all products and services of other corporations on whose board the director serves or to which he or she is a nominee; (4) requires A-M to notify the Commission of any proposed assignment, sale, or the like which may affect compliance with the order; and (5) requires filing of a report within 90 days as to the manner and form in which A-M has complied with the order.

The adjudicative hearings in the case-in-chief involving the remaining respondents, TRW and Mr. Shepard, were held in Cleveland, Ohio, and Los Angeles, California, from July 18 - 27 and July 29 - August 1, 1977, respectively. Hearings in the case-in-defense were held in Cleveland from August 22 - 29, 1977. Complaint counsel presented the case-in-rebuttal in Cleveland on September 2, 1977. The official record consists of 2477 pages of transcript. There are 111 numbered exhibits. Of these, 35 were rejected; however, in accord with Commission Rule 3.43(g), they remain a part of the official record. [**6**]

Bases for the Findings of Fact; Abbreviations Used

The findings of fact following are based on a review of the allegations made in the complaint, respondents' answers, the documentary evidence, and consideration of the demeanor of the witnesses. In addition, the proposed findings of fact, conclusions and proposed orders, together with reasons and briefs in support thereof filed by each side have been given careful consideration. To the extent not adopted by this decision in the form proposed or in substance, they are rejected.

For convenience, the findings of fact include references to supporting evidentiary items in the record. Such references are intended to serve as guides to the testimony, evidence and exhibits supporting the findings of fact. They do not necessarily represent complete summaries of the evidence considered in arriving at such findings. The following abbreviations have been used:

Tr. – Transcript, preceded by the names of the witness and followed by the page number.

CX – Commission's Exhibit, followed by its number.

RX – Respondents' Exhibit, followed by its number.

CCPF and CCB – Complaint Counsel's Proposed Findings and Brief

RPF and RB – Respondents' Proposed Findings and Brief.

[7] Note: The transcript in this proceeding was not paginated consistently. In order to locate citations to the transcript it may be helpful to use this table. The left hand column alphabetically lists the witnesses and the right hand column gives the date(s) on which he testified. Transcript volumes correspond to the dates of testimony.

Witness Name	Date Testified
Barney	July 29, 1977
Bender	July 22, 1977
Benton	August 26, 1977
Bryan	July 25, 1977
Bauchwitz	August 29, 1977
Close	August 25, 1977
Creekmore	July 19, 1977
Davis	August 23, 1977
Dougherty	July 29, 1977
Dugan	September 2, 1977
Fleming	July 26, 1977
Gorman	August 23, 1977
Guthrie	July 20, 1977
Kaplan	July 21, 1977
Kovar	August 24, 1977
Mattes	July 27, 1977
Mettler	August 22, 1977
Munyon	August 24–25, 1977
Murphy	August 23, 1977
Noel	July 18, 1977
Oie	August 1, 1977
Overmire	August 1, 1977
Peterson	September 2, 1977
Schmidt	July 19, 1977

Schwartz	September 2, 1977
Shepard	August 22, 1977
Solganik	September 2, 1977
Turley	September 2, 1977
T. Walsh	July 27, 1977
W. Walsh	July 27, 1977
Weber	July 29, 1977
Weedon	July 26, 1977
Wolfson	July 20, 1977

[8] FINDINGS OF FACT

I. The Parties

A. Respondent TRW, Inc.

1. TRW, Inc. (hereinafter TRW) is a publicly held corporation organized and existing under the laws of the State of Ohio. TRW is headquartered at 23555 Euclid Ave., Cleveland, Ohio. (Answer of TRW, ¶ 2).

2. TRW and its subsidiaries are principally engaged in the design, manufacture and sale of products for industry and government, and for the performance of advanced systems engineering, research and technical services in electronics and computer based services, domestic car and truck products, international car and truck products, car and truck replacement parts, spacecraft and propulsion products, fasteners, tools and bearings and energy products and services. TRW, during this proceeding, owned and operated plants in the United States, Europe, South America, Australia, Canada, Mexico, Africa, Taiwan and the United Kingdom (Moody's Industrial Manual, 3024-30, 1977 ed.).

3. In fiscal 1974, TRW had total current assets of $960,233,000, net sales and revenues totaling $2,486,022,000 and net income of $254,352,000. In fiscal 1975, TRW had total current assets of $897,592,000, net sales and revenues totaling $2,585,683,000 and net income of $263,903,000 (Moody's Industrial Manual, 3024-30, 1977 ed.).

4. On April 23, 1974, TRW acquired Financial Data Services, Inc. (hereinafter FDSI) (CX 180; CX 182).

5. TRW, at all times pertinent to this proceeding, engaged in commerce as defined in Section 1 of the Clayton Act [15 U.S.C. 12 and Section 4 of the Federal Trade Commission Act [15 U.S.C. 4 (Answer of TRW, ¶ 2; Finding 2).

6. TRW, at all times pertinent to this proceeding, had capit

surplus and undivided profits aggregating more than one million dollars (Answer of TRW, ¶ 2; Finding 3). [9]

B. Addressograph-Multigraph Corporation

7. Addressograph-Multigraph Corporation (hereinafter A-M) is a publicly held corporation organized and existing under the laws of the State of Delaware. A-M is headquartered at 20600 Chagrin Boulevard, Shaker Heights, Ohio. (Answer of A-M, ¶ 3).

8. A-M and its subsidiaries manufacture and sell an extensive line of name-and-data writing, office duplicating and offset duplicating machines and apparatus. A-M, during this proceeding, operated some 38 plants in the United States, Canada, Mexico, Europe, Africa, Japan, Australia and New Zealand (Moody's Industrial Manual, 1108–09, 1977 ed.).

9. In fiscal 1974, A-M had net current assets of $147,799,000, net sales and revenues totaling $540,833,000 and net income of $308,000. In fiscal 1975, A-M had net current assets of $150,930,000, net sales and revenues totaling $584,246,000 and net income of $4,908,000 (Moody's Industrial Manual, 1108–09, 1977 ed.).

10. A-M, at all times pertinent to this proceeding, engaged in commerce as defined in Section 1 of the Clayton Act [15 U.S.C. 12], and Section 4 of the Federal Trade Commission Act [15 U.S.C. 44] (Answer of A-M, ¶ 3; Finding 8).

11. A-M, at all times pertinent to this proceeding, had capital, surplus and undivided profits aggregating more than one million dollars (Answer of A-M, ¶ 3; Finding 9).

12. A-M, by a consent decision and order dated August 11, 1977 [*supra*], withdrew from adjudication prior to this hearing.

C. Respondent Horace A. Shepard

13. Following a distinguished military career, Horace A. Shepard, in 1951, joined TRW as Vice President and Assistant to the General Manager. Shepard became President of TRW in 1962 and Chairman and Chief Executive Officer in 1969 (Shepard, Tr. 849, 850–52). [10] First elected to TRW's Board of Directors in 1957, Mr. Shepard has served continuous three-year terms from that date to the present. Mr. Shepard, due to TRW's mandatory retirement at age 65 policy, retired as Chief Executive Officer on November 30, 1977. Mr. Shepard, however, is permitted to remain on the TRW Board until his seventy-second birthday (Shepard, Tr. 852; CX 181).

14. Horace A. Shepard was initially elected to the A-M Board of Directors on March 20, 1971 (Shepard, Tr. 874; Davis, Tr. 1158). Mr.

Shepard served on the A-M Board through November 6, 1975 (Shepard, Tr. 884; Answer of A-M, ¶ 4).

15. Horace A. Shepard served on both the A-M and TRW Boards of Directors from March 20, 1971, through November 6, 1975 (Findings 13-14).

II. The Alleged Interlock

A. How Horace A. Shepard Came To Sit on the A-M Board

16. In 1970, Charles L. Davis was offered and, in 1971, assumed the Presidency of A-M (Davis, Tr. 1154). Charles L. Davis and Horace A. Shepard had enjoyed a friendship dating back to and beyond the period when Shepard was Davis' commanding officer at Wright-Patterson Air Force Base in Dayton, Ohio (Davis, Tr. 1153; Shepard, Tr. 853-54). After having been offered the Presidency of A-M, Davis, in the course of deciding to accept the position, sought out Shepard's advice (Shepard, Tr. 856-58; Davis, Tr. 1154-55). Even while weighing A-M's offer, Davis entertained hopes that Shepard could be persuaded to join the A-M Board (Davis, Tr. 1155-56; Shepard, Tr. 858-59). Because of his desire to have directors of the A-M Board whom he could trust as well as his general lack of familiarity with the Cleveland business community, Davis, after assuming the A-M Presidency, continued to press the A-M directorship upon Shepard (Davis, Tr. 1156-57; Shepard, Tr. 860). Shepard finally agreed to join the A-M Board with the understanding that he would serve as a director only for a five-year period, during which time Davis hoped to reverse A-M's fortunes (Davis, Tr. 1157; Shepard, Tr. 858, 860). [11]

17. Horace A. Shepard, for his own part, was initially reluctant, due to his other responsibilities, about accepting the position on the A-M Board (Davis, Tr. 1155-56; Shepard, Tr. 859). Before agreeing to become an A-M director, Shepard conferred with Eugene Ford, then TRW's General Counsel, and Dr. Rueben Mettler, then President but now Chief Executive Officer of TRW. TRW's General Counsel "examined all of the relevant facts" and concluded that Shepard could join the A-M Board (Gorman, Tr. 1023; Shepard, Tr. 862-64, 927). Mettler, because of Shepard's busy schedule and a belief that an A-M directorship was of no benefit to TRW, advised Shepard against joining the A-M Board (Mettler, Tr. 933-34, 956, 963). It should be noted that, although TRW now employs an extensive screening process to avoid Clayton 8 problems (Gorman, Tr. 1029-42; RX 4; *see also* RX 58, RX 59), the procedure in 1971 was rather less well developed (Gorman, Tr. 1024), so much so that the TRW Board

was never notified—either by Shepard or anyone else—that Shepard had joined the A-M Board (Mettler, Tr. 934; Shepard, Tr. 861-62).

18. There is no indication that TRW in any way promoted or took corporate action sanctioning Shepard's assumption of the A-M directorship (Findings 16-17).

B. Other Alleged Interlocks Involving Horace A. Shepard and TRW

19. In 1967, while serving on the Boards of TRW and Midland-Ross Corporation, Horace A. Shepard was the object of a Section 8 investigation conducted by the Department of Justice. Shepard himself had the question of overlapping TRW and Midland-Ross products researched with the conclusion of no overlap. Nevertheless, the Department of Justice requested that Shepard resign from either the TRW or Midland-Ross Board. Shepard, in order to save the two corporations legal expenses and adverse publicity, resigned from the Midland-Ross Board. The Department of Justice then closed the investigation without filing a complaint (Shepard, Tr. 864-68; CX 208, CX 208-A, CX 208-E to K, CX 208-O, CX 208-V). [12]

20. In 1968, Shepard was asked to join the Board of White Motor Company. Shepard requested and was denied a "railroad" clearance (*i.e.*, the submission of a question to the Justice Department with a request for an advisory opinion as to the legality under the antitrust laws of a course of action, Weedon, Tr. 363). As a result of the denial, Shepard refused the White Motor directorship (Shepard, Tr. 869-73; Gorman, Tr. 1015-16; Weedon, Tr. 365, 367, 370; CX 210).

21. In 1971, Shepard, while serving on the Boards of TRW, A-M and Harris-Intertype Corporation, was again the subject of a Department of Justice Section 8 investigation. On the basis of studies conducted by the three corporations, Shepard concluded that no product overlap existed (Shepard, Tr. 874-78). In a meeting which occurred in Cleveland in the summer of 1971 between Justice Department officials and TRW counsel, it was made clear that the area of concern was the possibility of product overlap between A-M and Harris. Further, the Department of Justice had concluded that TRW and A-M were not competitors (Gorman, Tr. 1017-21; Weedon, Tr. 353, 356, 361; CX 211-A - B; *see also* RX 56; RX 57; and Gorman, Tr. 1021-23 on the question of any possible ambiguity about the understanding of that meeting and its commitment to writing). Shepard subsequently resigned from the Harris Board (Gorman, Tr. 1021). Shepard regarded the investigation and its resolution as "in fact a clearance to continue as director of both TRW and Addressograph-Multigraph" (Shepard, Tr. 878).

22. On July 26, 1974, Shepard resigned from the Board of Diamond Shamrock Corporation. Shepard had previously been notified that the Federal Trade Commission intended to file a complaint against Diamond Shamrock and the Standard Oil Company for alleged violations of Section 8 (Shepard, Tr. 923-24; Weedon, Tr. 381, 384; CX 212; CX 213 to CX 213-O; CX 214 to CX 214-O). [13]

III. The Products

A. The TRW System 4000/5000

23. *Generally:* Throughout the complaint period, TRW's key product, for purposes of this proceeding, was its System 4000/5000 (Bauchwitz, Tr. 1838). Although the System 4000 was marketed apart from the System 5000, the two systems were essentially one and the same. The System 4000 was designed as a credit authorization system (on "credit authorization" *see* T. Walsh, Tr. 543-44; Bryan, Tr. 246) for department store house accounts (Bauchwitz, Tr. 1810-11, 1843; Kovar, Tr. 1230, 1244; Close, Tr. 1547-48; CX 167). The design of the System 5000 concentrated upon the credit authorization needs of banks and other financial institutions (Bauchwitz, Tr. 1886; Kovar, Tr. 1230; CX 158; CX 172). Both systems were optimally suited to environments characterized by the need for clusters of terminals and a high volume of transactional traffic (Kovar, Tr. 1226, 1228, 1283; Bauchwitz, Tr. 1811; Bryan, Tr. 280; Close, Tr. 1546-58; Findings 24-25, *infra*).

24. *System Features:* The TRW System 4000/5000 used, during the complaint period, the 4103 terminal (Kovar, Tr. 1231-33; *see generally* CX 201). Designed to occupy as little retail counter space as possible, the functions of the 4103 were limited to the clerk's use of the keyboard to transmit information and the receipt and display of the computer's answer (Kovar, Tr. 1234-35). The 4103 terminal lacked both a printer, a device applying text or numbers to a page in response to an electrical impulse, and imprinter, a device transferring raised characters to an inked piece of paper, as well as the ability to communicate directly with a computer (Kovar, Tr. 1231-32, 1271). In order to communicate over a telephone line with a central computer, the 4103 terminal had to be used in conjunction with a controller (Kovar, Tr. 1235-36). The controller was itself composed of a scanner control, which monitored the various terminals attached to the controller, and the modem, which converted the keypad signal to telephone use (Kovar, Tr. 1238, 1240-41; Close, Tr. 1549). Through the use of the special capabilities of the store located controller, as many as 128 4103 terminals could be simultaneously controlled. The

effect of this arrangement was to distribute the costs of the controller and host computer among many terminals in a single store location (Kovar, Tr. 1240; Bauchwitz, [14] Tr. 1811-12). The 4103 terminal could be upgraded to include an imprinter, card reader and customer identification pads. However, these items would be included alongside and not in the terminal housing (Kovar, Tr. 1334-36).

25. *System Uses:* The envisioned use of the System 4000/5000 in a multi-clustered terminal environment was borne out in fact. During the complaint period, 70-75 System 4000's—and some 60,000 credit authorization terminals—were sold or leased to American department stores (Bauchwitz, Tr. 1813, 1893). Ninety percent of all System 4000 revenues came from department store sales and leases (Bauchwitz, Tr. 1813).

B. The TRW Validata System

26. *Generally:* TRW's Validata System involved the sale of a service rather than mechanical system (Kovar, Tr. 1253). Validata provided the service of verifying transactions involving credit cards, checks and lost or stolen airline tickets (Bryan, Tr. 245, 276). In contrast to credit authorization (*see* Finding 23, *supra*), credit verification calls for a search of a "negative" file containing those accounts not to be honored. Validata's "negative" file was drawn from data supplied by, among others, Master Charge, American Express, Diner's Club, Carte Blanche and BankAmericard (Bryan, Tr. 247-48). Validata was designed for use in the clustered or multi-terminal environment. Airport terminals were considered to be particularly appropriate sites (Kovar, Tr. 1254), but Validata also was advertised for use in shopping malls (Kovar, Tr. 1326-27).

27. *System Uses:* Airlines and national car rental agencies were the major subscribers to the Validata service (Bauchwitz, Tr. 1820, 1827; Bryan, Tr. 245, 279). Indeed, 95 percent of all Validata revenues came from airlines and car rental agencies (Bryan, Tr. 279). Validata proved unworkable for shopping malls because of that type of facility's inability to impose upon its tenants the degree of control exercised by airline terminals (Kovar, Tr. 1256). Validata was used in other than multi-clustered environments as an accommodation to some customers but not frequently (Kovar, Tr. 1320-23). [15]

C. FDSI Terminals

28. On April 23, 1974, TRW acquired FDSI (Finding 4, *supra*). FDSI devices were predominantly large machines designed for use in

banks and savings and loans (Kovar, Tr. 1262–63; Bauchwitz, Tr. 1875). The principal FDSI terminals offered for sale during the complaint period are described in Findings 29–31, *infra*.

29. The FDSI TT-115, which lacked an imprinter, was designed for consumer use in the very specialized environment of a supermarket check stand (Kovar, Tr. 1265; CX 159). The TT-115 System operated along lines very similar to those of the TRW System 4000 (Close, Tr. 1592). The TT-115 was the only TRW or FDSI device which contained a magnetic stripe card reader (Kovar, Tr. 1267). In addition, the TT-115 featured, in order to provide security to the consumer user, a Personal Identification Number (PIN) used in conjunction with the terminal keyboard (PIN pad) (Kovar, Tr. 1264–65; Bauchwitz, Tr. 1831; CX 163). The TT-115 was designed for and sold only to Glendale Federal Savings and Loan for use in the Smith Food King Chain (Kovar, Tr. 1269; *see also,* Findings 39–42, *infra*). During the complaint period, the TT-115 cost $1,675 (Bauchwitz, Tr. 1907). William J. Bauchwitz, a planning staff member of TRW's Communications Systems and Services Division, indicated that the per terminal economics of the TT-115 and AMCAT I were, in some circumstances, comparable (Bauchwitz, Tr. 1909). This parity of economies could be upset, however, by the specific needs of an individual buyer (Bauchwitz, Tr. 1910–14).

30. FDSI, under the auspices of TRW, also produced some 10 prototype models of the TT-116 (Bauchwitz, Tr. 1864). The ability of the customer to insert a check for validation into the terminal was the distinctive feature of the TT-116 (Kovar, Tr. 1299–1301; Bauchwitz, Tr. 1861; CX 104-Z-17). The TT-116 prototype models were shown to Wells Fargo (Kovar, Tr. 1310). **[16]**

31. During the complaint period, FDSI produced foam board mock up models only of the TT-117. The TT-117 was meant to perform credit authorization, check validation and other electronic funds transfer functions at supermarket cash register counters (Bauchwitz, Tr. 1864–65; CX 104-Z-18; CX 104-Z-19; CX 244-Z-29; CX 244-Z-31).

D. The AMCAT I

32. *Generally:* A-M had long been in the business of supplying gasoline companies with Zip-Zap machines (invoice and receipt imprinting devices) for use in credit card sales. Because of the increasing losses suffered by the oil companies due to credit card fraud, A-M developed a device, the AMCAT I, for transmitting requests and receiving credit authorization information (Cady, Tr. 1713–15). Although A-M's hopes for marketing the AMCAT I were

not realized (Cady, Tr. 1711–12), the AMCAT I was utilized by some gasoline service stations and small retail stores (*see* Finding 34, *infra*).

33. *System Features:* In contrast to the TRW System 4000, the AMCAT I integrated many of the credit authorization system components into the terminal itself. The inclusion of a modem in the AMCAT I created a "stand alone" terminal. That is to say, the AMCAT I was capable of communicating with a host computer through a specially leased telephone line without the use of a controller or any other externally located piece of equipment (Cady, Tr. 1703–04; Kovar, Tr. 1274; CX 245-Z-97). The AMCAT I, as a result of its integrated nature, was substantially larger than the TRW 4103 Kovar, Tr. 1257; CX 245-Z-93). The AMCAT I was capable of reading either magnetic stripe or raised character plastic cards. The AMCAT I also had a display and imprinter/printer device which allowed it to print a receipt from a plastic card (Cady, Tr. 1703, 1756). **[17]**

34. *System Uses:* Between January of 1973 and November 6, 1973, AMCAT I's were used predominantly in a "stand alone" environment, *i.e.,* one or two isolated terminals in a relatively small retail establishment (Cady, Tr. 1756–57; Close, Tr. 1568, 1612). Where large retail stores could establish their own system of credit authorization and in-house credit cards, it was not feasible for small retail shops to develop their own credit systems. Small stores tended to look to third party extenders of credit, such as American Express Company, to supply a fully developed electronic credit authorization plan (Close, Tr. 1564, 1584). Small stores, as a result, needed a credit authorization terminal possessing magnetic stripe card reading capabilities since the magnetic stripe card was commonly used by third party credit extenders (Close, Tr. 1570). Moreover, the small retail store favored the integrated terminal for this device reduced modem and phone line costs (Close, Tr. 1565). The AMCAT I, which answered all of the above demands, was accordingly utilized by third party extenders of credit, most notably American Express (Close, Tr. 1583; Cady, Tr. 1721). During the complaint period, AMCAT I's were not used by department stores, airlines, car rental agencies or in financial institutions as teller machines (Cady, Tr. 1752–58; Murphy, Tr. 1178, 1205–06).

E. Other A-M Products

35. During the critical period, any other relevant A-M products were largely variations on the AMCAT I. The AMCAT IC, which was utilized primarily in the First National Bank of Atlanta's "Honest Face" electronic transfer of funds program (*see* Findings 42–46,

infra), was an adaption of the AMCAT I which accepted checks and featured a consumer operated terminal (Cady, Tr. 1726–31; CX 195-V; CX 245-Z-96). The AMCAT 2 (CX 245-Z-93) differed from the AMCAT I in its ability to be used in a dial-up telephone system rather than having to be tied to a dedicated telephone line. This modification in the AMCAT I was prompted by the special needs of the oil companies and [18] their service stations. However, apparently very few, if any, AMCAT 2's were actually sold (Cady, Tr. 1724–26). The MODCAT and HALFCAT terminals were pared down versions of the AMCAT I. Although shown to potential buyers, these variations on the AMCAT I were apparently never produced in other than cardboard model form (Cady, Tr. 1741–44).

IV. Credit Authorization System Transactions Occurring During the Critical Period

A. The Electronic Funds Transfer Market Generally

36. The outstanding feature of the so-called electronic transfer of funds systems marketplace during the complaint period was its highly experimental and developing state (Benton, Tr. 1689; W. Walsh, Tr. 427; Creekmore, Tr. 33; Noel, Tr. 137; CX 171). The general description of electronic transfer of funds can be broken into three rather more specific categories: the authorization of credit card transactions, the verification or guaranteeing of checks, and the true transfer of funds, *i.e.,* deposits and withdrawals from savings or checking accounts. Indicative of the industry's highly fluid state was the proliferation of systems of different functional capabilities and engineering design. Various systems produced by numerous manufacturers could accomplish one, two or all of the above-named functions (Noel, Tr. 120). Systems, even when similar in the end function performed, were frequently dissimilar in their method of accomplishing that final result (Noel, Tr. 118–20).

37. The following factors were generally agreed to have been taken into account by potential electronic funds transfer systems purchasers: (1) the geographic dispersion of points of sale, *i.e.,* a department store with many points of sale within that store as opposed to a system of gasoline stations, (2) the physical location of terminals including the amount of space allotted per terminal, *e.g.,* the difficulties posed by fitting a terminal into a supermarket check stand, (3) the anticipated transactional volume, (4) the type of credit card and credit system used, *i.e.,* in-house as opposed to a third party credit system, (5) the specific jobs which the terminal was expected

to do, *e.g.,* imprinting and printing capability and (6) the cost of the system (Bauchwitz, Tr. 1577; Bryan, Tr. 273–74). [19]

B. Specific EFT Purchase Transactions

38. *Glendale Federal Savings & Loan Association:* On November 19, 1974, the Board of Directors of the Glendale Federal Savings & Loan Association, pursuant to a proposal made to the Federal Home Loan Bank Board approved a proposal for placing a number of electronic funds transfer terminals in Southern California supermarkets (Barney, Tr. 650–51). The goal of the Glendale Federal proposal was to set up facilities permitting the acceptance of deposits to and the authorization of withdrawals from savings and checking accounts at retail food store checkout stands (Barney, Tr. 648). In implementing this plan, Glendale Federal desired a terminal small enough to fit into the restricted space of a supermarket check stand, keyboard and digital display, a magnetic stripe card reader and a personal identification number pad (PIN pad) (Barney, Tr. 653–55, 658–60).

39. Donald J. Barney, Manager of the Information Systems Division of Glendale Federal, personally contacted TRW, NCR, Burroughs and IBM in late June or early July of 1974 to inquire whether those firms had equipment capable of meeting Glendale Federal's requirements. In addition to those firms solicited, Glendale Federal stood willing to submit its system specifications to any other interested manufacturer. Glendale Federal was approached by representatives of A-M in either late July or early August of 1974. On August 26, 1974, Mr. Barney visited A-M's Los Angeles branch and witnessed a demonstration of the AMCAT terminal (Barney, Tr. 651–52). No manufacturer, whether or not solicited, had equipment that would do what Glendale Federal wanted it to do in the fashion desired (Barney, Tr. 653). The AMCAT, for instance, did not operate at a sufficient baud rate (the rate of communicating from the terminal to the computer) so that the rate of communication was too slow for an adequate service response, the A-M Communication Network required the use of an expensive control unit to gain compatability with the central processing unit, the AMCAT terminal was too large to fit on the check-out stand, and A-M did not offer a PIN pad to insure proper user security (Barney, Tr. 652–55). [20] The TRW 4103 was found to have "the same limitations" such as the lack of a magnetic card reader. However, the 4103 fit the check stand (Barney, Tr. 658). Despite the common deficiencies, Mr. Barney testified "it was clear to me that no manufacturer except TRW was going to be able to design and build a piece of gear and deliver it in

our time frame, for the installation of the original 200 machines" (Barney, Tr. 655; *see also* CX 227-Z-65, CX 227-Z-67). A-M persisted in attempting to sell to Glendale Federal, but never submitted a formal proposal (Barney, Tr. 656, 686; RX 23).

40. TRW began development work on a terminal specially designed for Glendale Federal, the TT-115, in the fall of 1974, negotiated an agreement with Glendale Federal at the end of November 1974 and executed a formal contract of purchase in March of 1975. TRW began delivering completed TT-115's in May of 1975. The first installation of a TT-115 terminal in a Glendale Federal system supermarket occurred on August 23, 1975 (Barney, Tr. 650–52).

41. Some time between February 28 and March of 1975, A-M showed Glendale Federal the MODCAT (Barney, Tr. 656–57). The MODCAT appeared to fit Glendale Federal's specifications of the year before; however, in March of 1975, Glendale was not in the market for a terminal (Barney, Tr. 658).

42. *First National Bank of Atlanta:* The First National Bank of Atlanta, Georgia, had developed an electronic check verification and factoring (*i.e.,* the buying of accounts receivable created by written checks from retail establishments) system. The so-called "Honest Face" system allowed consumer check verification or factoring to take place, by means of a point of sale terminal, at the retail establishment itself (Creekmore, Tr. 11–12). The consumer issued an "Honest Face" card operated the point of sale terminal, which verified or factored the consumer's check. Because the terminal was to be consumer operated, First National of Atlanta insisted that the terminal be equipped with an operator lead through, or prompter device, which would lead the consumer through his use of the terminal (Creekmore, Tr. 67–68). Because the "Honest Face" system was to be activated by a specially issued card, the terminal had to have the capability of reading a magnetic stripe card. Finally, in order to actually verify the check, the terminal had to have [21] an imprinter (Creekmore, Tr. 68–69). Although it was envisioned that "Honest Face" terminals would be installed in all types of retail stores, at the close of 1975 some 375 terminals had been placed only in grocery stores, liquor stores and other stand-alone locations. "Honest Face" terminals were not placed in a major retail store because those stores had too many point of sale locations and because large stores had their own electronic cash registers (Creekmore, Tr. 37–38, 73).

43. In its search to find a manufacturer willing to devise a system featuring a shopper operated terminal, First National Bank contact-

ed 37 electronic terminal vendors, including A-M and TRW (Creekmore, Tr. 59–60). Robert P. Creekmore, the First National Bank of Atlanta, Georgia officer who headed up the Honest Face Program, testified that all terminal vendors balked at developing a shopper operated terminal (Creekmore, Tr. 59).

44. Although TRW never submitted a formal bid, (Creekmore, Tr. 77), Mr. Creekmore testified that "over our period of discussions they [TRW] offered to make certain modifications in new products, that in effect would give partial answers to some of the needs that we had in the terminal we desired" (Creekmore, Tr. 65). However, First National of Atlanta's talks with TRW finally broke down because of TRW's inability to develop a satisfactory shopper operated terminal (Creekmore, Tr. 76–78; Bauchwitz, Tr. 1848).

45. A-M, initially, had neither the hardware to satisfy First National of Atlanta's needs nor the willingness to modify their existing equipment. A-M so opposed First National's idea that a customer operated terminal was desirable and feasible that First National, for a time, angrily refused to have any further discussions with A-M representatives (Creekmore, Tr. 81; Cady, Tr. 1729). A-M subsequently warmed to the idea of the prompter device, developed the AMCAT IC (*see* Finding 35, *supra*) and negotiations between A-M and First National were resumed (Cady, Tr. 1730; CX 193-V). [22]

46. A-M's willingness to meet First National's requirements combined with the unwillingness of the other terminal vendors, allowed A-M to secure, by February of 1975, the "Honest Face" contract (Creekmore, Tr. 77, 81).

47. *Metroteller/Erie County Savings & Loan, Erie, Pa.:* Metroteller (or Consumer Save System Corporation and Consumer Service Corporation as it was known during the critical period) was a wholly-owned subsidiary of the Erie County Savings Bank (Wolfson, Tr. 21). Metroteller existed to develop remote banking facilities, *i.e.,* a facility which would allow a customer of a financial institution to make savings and checking account deposits and withdrawals while in a retail establishment (Wolfson, Tr. 20–21, 33–35). Metroteller provided this service not only to its parent, but to other local financial institutions (Wolfson, Tr. 25).

48. In October of 1974, Erie County Savings Bank began a search for a point of sale terminal. Joseph Wolfson, President of Metroteller, described the search as a process of contacting many terminal vendors and then narrowing the field as it became apparent which suppliers were offering products well suited to Erie National's requirements (Wolfson, Tr. 26–27). Among the half dozen vendors

contacted by Metroteller were A-M and TRW's FDSI division (Wolfson, Tr. 25; Bauchwitz, Tr. 1874-75).

49. Beginning in July of 1974 and through the end of 1975, Metroteller met with TRW and FDSI representatives to discuss the suitability of TRW and FDSI products as remote banking terminals. Metroteller was shown the TT-108. Metroteller officials were taken to California to observe the TT-115's used by Glendale Federal (Wolfson, Tr. 45-47, 49-50, 53). The TT-140, which Metroteller eventually purchased, was not shown during the critical period (Bauchwitz, Tr. 1880).

50. At the same time that Metroteller was being shown TRW's products, A-M was also attempting to sell their AMCAT I and 2 to Metroteller (Wolfson, Tr. 60-61, 63-64). Because of programming costs as well as expense in adapting Erie National's existing system to the AMCAT terminals, Metroteller did not purchase any of the A-M terminals (Wolfson, Tr. 64-67). [23]

51. *Buckeye Federal Savings & Loan, Columbus, Ohio:* During the critical period, Buckeye Federal implemented a remote service unit terminal program. It was anticipated that terminals, located in retail stores, would be able to make deposits, withdrawals, confidential inquiries and guarantee checks (Guthrie, Tr. 86, 87, 91-92). Buckeye decided that it was interested in securing a terminal possessing the capability to print a receipt, a ten key pad—so that a customer could utilize a personal security code—a magnetic stripe card reader and an imprinter (Guthrie, Tr. 119-20).

52. Buckeye initially attempted to contact "anybody we could think of who had a credit authorization device or was in the terminal business" (Guthrie, Tr. 103). A-M and TRW were among the manufacturers contacted by Buckeye Federal (Guthrie, Tr. 103, 110). A-M was the only vendor with a terminal integrating all of the above-described functions. Nevertheless, TRW made some efforts or representations of efforts, of attempting to modify their product to meet Buckeye's goals. Stephen Guthrie, Buckeye's Senior Vice President for Marketing and Data Processing, testified that FDSI and TRW products were never seriously considered (Guthrie, Tr. 120).

53. Buckeye eventually installed AMCAT terminals on April 21, 1975 (Guthrie, Tr. 91). Terminals have subsequently been installed at supermarket offices and courtesy windows, and discount stores (Guthrie, Tr. 93, 96).

54. *Credit Systems, Incorporated (CSI):* Credit Systems, Incorporated, of St. Louis, Missouri, was a processing center for 785 banks handling Master Charge and Visa cards (Bender, Tr. 194). In April of

1974, CSI began to formulate the design for a system which would handle check guarantees for retail stores at the point of sale and act as an automatic teller for financial institutions (Bender, Tr. 197, 201). The terminals developed were intended to be used in both banks and retail outlets (Bender, Tr. 200). [24]

55. In order to realize their system design, CSI conducted a study of electronic transfer of funds manufacturers. The study's purpose was to ascertain the universe of manufacturers and the particular computer hardware produced by each (Bender, Tr. 202-03). As a result of their survey, CSI classified potential point of sale terminal vendors into one of three categories: (1) mechanical reader with automatic printer/imprinter, (2) mechanical reader, non-printing, and (3) manual input. A-M was placed in the first classification, TRW in the last. Neither A-M nor TRW was listed under the mechanical reader, non-printing category (Bender, Tr. 220-22).

56. CSI, during the critical period, sent out requests for quotation to all manufacturers (CX 102), whatever their category, for a point of sale terminal (CX 101). Both A-M and TRW responded to CSI's request for quotation (CX 103; CX 104). Although TRW admitted in its response that its terminal lacked a printing capability, TRW stated that it expected to have such capability by the fall of 1976 (Bender, Tr. 222-23; CX 104-Z-4-5). TRW's response, nevertheless, talked of the "excellent match" between CSI's needs and TRW's equipment (CX 104-F). Because of legislative and regulatory action, CSI did not actually purchase any terminal (Bender, Tr. 213-14). However, Jay Bender, President of Systems Service for CSI, testified that TRW's present inability to supply a terminal with printing and imprinting capacity made TRW's response unsatisfactory (Bender, Tr. 228, 233; Bauchwitz, Tr. 1848).

57. *American Express:* During the complaint period, American Express Company was the major purchaser of AMCAT terminals (Cady, Tr. 1721). This situation was the result of both a good relationship between American Express and A-M (Cady, Tr. 1718-19) and the suitability of the AMCAT terminal to American Express needs (Cady, Tr. 1719-20; Bryan, Tr. 281-82; Finding 33, *supra*). Peter Bryan, an Executive Vice President of Payment Systems, Inc., a subsidiary of American Express, and a former TRW employee, testified that American Express never seriously considered TRW's terminal. American Express, however, did go to the trouble of assessing whether TRW's product would answer American Express' needs (Bryan, Tr. 282). [25]

58. *Virginia Federal Savings & Loan, Richmond, VA.:* From 1974, Virginia Federal Savings & Loan began considering the purchase of

terminals for a remote unit system similar to that created by Buckeye Federal (Fleming, Tr. 394, 397, 404; *see* Finding 51, *supra*). Virginia Federal, though it ultimately purchased the AMCAT terminal, had no contact with A-M representatives prior to November 6, 1975 (Fleming, Tr. 407). Virginia Federal was aware, however, of the existence of the AMCAT and its use by California Federal Savings and Loan (Fleming, Tr. 395; see Findings 60–61, *infra*). During the November 1974 - March 1975 period, Virginia Federal discussed the suitability of TRW's terminals for the Virginia Federal System (Fleming, Tr. 400–03). The TRW product performed many, but not all, of the functions desired by Virginia Federal (Fleming, Tr. 402–04). Even the AMCAT, which met most of Virginia Federal's demands, was unable to produce receipts (Fleming, Tr. 404–05). The major objections of Virginia Federal to TRW were the difficulties in servicing and the expense of the TRW system due to the fact that a mini-computer would have been required for each location housing a terminal (Fleming, Tr. 402).

59. *Continental National Bank:* The Continental National Bank of Chicago, Illinois used the AMCAT in supermarkets to authorize charge account purchases, guarantee checks and for Master Charge transactions (T. Walsh, Tr. 543, 546). Continental did not consider any terminal other than the AMCAT (T. Walsh, Tr. 551).

60. *California Federal Savings & Loan, Los Angeles, CA.:* During the critical period, California Federal Savings & Loan placed electronic transfer of funds terminals, which were activated by plastic cards, at supermarket and liquor store locations. Customers holding California Federal cards could make deposits and withdrawals from their accounts and cash checks (Weber, Tr. 601). This initial system used the AMCAT I. This record contains no evidence about the competitive circumstances surrounding this purchase decision (Weber, Tr. 613). **[26]**

61. California Federal subsequently began to contemplate expansion of its original system. It wished to expand the terminal network into the Vons Grocery Store chain and hoped to place terminals at the check-out stand counter in addition to special courtesy booths (Weber, Tr. 614, 626–27). While this expansion was being planned, California Federal had discussions with TRW and A-M representatives about terminals suitable for check-out counter use. California Federal was told that the TRW 4103 terminal would function at either a courtesy booth or check-out counter. A-M represented that its MODCAT was suitable for check-out counter use (Weber, Tr. 627–28, 640–41; CX 302; CX 303). Due to the lack of a terminal with printing and imprinting capability, negotiations between TRW and

California Federal eventually broke down. TRW never submitted a formal bid (Bauchwitz, Tr. 1883–85).

62. *Bank of America, San Francisco, CA.:* As early as 1973, Bank of America had designed an experimental electronic transfer of funds system (Dougherty, Tr. 693–97). By 1975, Bank of America wanted to enlarge upon the original system. In July of 1975, Bank of America issued a request for information (CX 243-C to 243–Y) for terminals, controllers and subsystems necessary to support merchant point of sale operations. These requests for information were issued to some 29 vendors. Bank of America received responses from 10 of those 29 vendors, including A-M and TRW (Dougherty, Tr. 702, 710–11; CX 244; CX 245-A). It should be noted that Bank of America recognized a distinction between a request for information and a request for proposal. That distinction was that a request for information was used to determine available suppliers of equipment, characteristics of equipment and the ability of suppliers to meet generally basic requirements. By contrast, a request for proposal was viewed as a firm indication of the bank's intent to purchase some amount of equipment as a direct result of receiving responses (Dougherty, Tr. 728–29; CX 243-A). TRW replied to Bank of America's request for information. TRW officials testified that TRW was unable to meet Bank of America's specifications (Bauchwitz, Tr. 1889–93). Nevertheless, TRW's response, in its Executive Summary section, refers to "the excellent match between our equipment and the capabilities and system requirements defined in your RFI" (CX 244-K). Later in TRW's response, the following statement appears: "The requirement-by-requirement comparison which follows indicates an excellent match between Bank of America's requirements and the capabilities of TRW" (CX 244-Q). [27]

63. *Security Pacific Bank, Los Angeles, CA.:* During the critical period, Security Pacific Bank devised an electronic transfer of funds system utilizing magnetic stripe cards. These cards were "read" by terminals located in supermarkets. The terminals were to be connected via leased telephone lines with a central data base in Security Pacific's computer operations center (Oie, Tr. 737–38). Without a formal invitation, TRW representatives paid several visits to Security Pacific during the course of 1975. During these visits, TRW representatives loaned a TRW terminal to Security Pacific for a Security Pacific branch manager's show (Oie, Tr. 742–44). During 1975, A-M also visited Security Pacific. A-M's calls typically involved conversations with Security Pacific officials and leaving printed material describing the AMCAT terminal (Oie, Tr. 744–45). Security

Pacific ultimately purchased terminals from the Concord Computing Company (Oie, Tr. 740).

64. *Wells Fargo Bank, San Francisco, CA.:* During the critical period, Wells Fargo Bank developed Wells Service. Wells Service provided credit card authorization, check authorization and check guarantee to retailers (Overmire, Tr. 758). The decision of Wells Service to use TRW terminals was apparently made by default. Wells Fargo Bank did not consider any other vendors, including A-M, for Wells Service (Overmire, Tr. 761, 776).

65. However, Wells Fargo Bank, also during the critical period, considered developing an electronic transfer of funds system for supermarkets (Overmire, Tr. 761). Wells Fargo talked to TRW personnel over the last half of 1975 about the development of suitable terminals (Overmire, Tr. 761–64). TRW, as a result, developed prototypes for Wells Fargo. This involved modification of existing TRW terminals enabling the terminal housing to contain an imprinter with a slot into which a shopper could insert a check as well as electronic modification allowing the imprinter to print on the check (Overmire, Tr. 765–66). [28]

66. During 1975, Wells Fargo Bank also had contact with A-M regarding Wells Fargo's proposed expansion of electronic funds transfer services into the supermarket environment. Specifically, Wells Fargo looked at the AMCAT I. Mr. Peter Overmire, Vice President, Finance and Analysis Division of Wells Fargo Bank, testified that, in his opinion, the AMCAT I would have satisfied Wells Fargo's supermarket application needs. However, it was also Overmire's opinion that the AMCAT I was unduly cumbersome for check approval (Overmire, Tr. 766–67). It was eventually decided that the TRW terminal was to be used. However, Wells Fargo's supermarket application project never went beyond an internal experimental phase (Overmire, Tr. 768–69).

V. Respondents' Charges That Due Process Was Denied Them and That the Administrative Process Was Abused

67. By letter of August 8, 1975, the Federal Trade Commission first advised respondents of the investigation leading to the complaint in this matter. A proposed complaint accompanied the August 8 letter (Solganik, Tr. 1961–62; RX 54-A).

68. On September 8, 1975, counsel for respondents met with members of the Cleveland Regional Office of the Federal Trade Commission to discuss the August 8 letter and proposed complaint. Respondents, at the September 8 meeting, informed the Federal Trade Commission that Horace Shepard previously had decided not

to stand for re-election to the Board of Directors of A-M (Gorman, Tr. 1053; Solganik, Tr. 1965; RX 54-C), but Mr. Shepard told A-M that the Federal Trade Commission's letter was the reason for his decision not to stand for re-election (Shepard, Tr. 884–87). The next day, Mr. Thomas B. Clark, Secretary and Corporate Counsel of A-M, met with the Cleveland Regional Office staff to discuss a letter similar to that received by TRW on August 8, 1975, and an attached proposed complaint (CX 306-A and B; RX 54-D). Although Mr. Clark offered to provide the Commission staff with information about A-M's business and products, neither then nor at any other time prior to the service of the complaint did the Federal Trade Commission request information from A-M (Solganik, Tr. 2012; CX 306–A and B; RX 54–E). **[29]**

69. On October 31, 1975, the Federal Trade Commission requested from TRW information about dollar sales volume for certain TRW products, the date of TRW's acquisition of FDSI and a description of FDSI products. The October 31 letter, which was received by TRW on November 3, 1975, requested TRW to provide this data by November 7, 1975 (Gorman, Tr. 1086–87; CX 305-E). TRW informed the Federal Trade Commission that it would be unable to meet the requested date for submitting the three categories of data (Gorman, Tr. 1087). On November 14, 1975, the Cleveland Regional Office of the Federal Trade Commission forwarded to Washington, D.C., its recommendation that the complaint issue. At that time, respondents had not replied to the October 31, 1975 request for information (Solganik, Tr. 2020; RX 54-H to RX 54-H-1).

70. After learning about the forwarding of the recommendation, respondents requested and had a meeting with staff of the Federal Trade Commission in Washington, D.C., for the purpose of making a presentation as to why no complaint should issue (Gorman, Tr. 1056–57; Solganik, Tr. 1972–74). On December 10, 1975, a meeting was held in the Office of the Executive Director of the Federal Trade Commission. In attendance were Clinton Batterton, Assistant to the Director, Bureau of Competition, Federal Trade Commission; Robert Davidson, Counsel for TRW; John F. Dugan, Deputy Executive Director for Regional Operations, Federal Trade Commission; Joseph Gorman, Counsel for TRW; Lawrence Fox, Office of Regional Operations, Federal Trade Commission; Charles McCormick, Economist, Bureau of Economics, Federal Trade Commission; John M. Mendenhall, Law Clerk, Cleveland Regional Office, Federal Trade Commission; Richard Pogue, Counsel, Jones, Day, Reavis and Pogue, representing Shepard and TRW; Vivian L. Solganik, Assistant Regional Director, Cleveland Regional Office, Federal Trade Com-

mission; and Daniel Schwartz, Assistant Director for Evaluation, Bureau of Competition, Federal Trade Commission (Dugan, Tr. 2048–49; Solganik, Tr. 1974–75). At the close of the December 10 meeting, Mr. Gorman orally requested and received from Mr. Daniel C. Schwartz, the senior staff person present for the Federal Trade Commission, an assurance that TRW would be informed as soon as proposed complaint was forwarded (Solganik, Tr. 2026–28; Schwartz, Tr. 2032–33). [30]

71. Following the December 10, 1975, meeting, respondents next heard from the Federal Trade Commission some six months later, on June 25, 1976 (RX 54-M). By telephone call, Commission staff informed counsel for respondents that on June 17, 1976, the Federal Trade Commission had voted to direct the issuance of a complaint (Gorman, Tr. 1070; Peterson, Tr. 2067, 2071; RX 54-M; RX 55).

72. On July 9, 1976, respondents filed a motion for reconsideration of the issuance of the complaint and, in the alternative, urged the Federal Trade Commission, pursuant to Section 2.21 of the Commission's Rules of Practice, to accept an assurance of voluntary compliance from respondents (RX 53). On July 13, 1976, the Federal Trade Commission referred the motion to an administrative law judge for determination. The Commission itself refused to consider respondents' motion for reconsideration and related relief (RX 3-G; RX 54-U to RX 54-U-3; RX 55-A).

73. On July 22, 1976, respondents were served with the complaint and the presiding administrative law judge was identified (RX 40-D; RX 54-V).

74. The motion for reconsideration referred by the Federal Trade Commission to the administrative law judge was certified to the Federal Trade Commission by the administrative law judge in September of 1976 (88. F.T.C. 544 (1976)).

75. On October 13, 1976, the Federal Trade Commission denied TRW's motion for reconsideration (88 F.T.C. 544 (1976)). [31]

Discussion

The Case Is Not Moot Even Though the Interlock Was Dissolved

Respondents argue that Mr. Shepard's decision not to stand for re-election to the A-M Board of Directors moots this proceeding. Administrative tribunals are not under the "case or controversy" constitutional constraint federal courts are (U.S. CONST. art. III, § 2; *Powell* v. *McCormick,* 395 U.S. 496 n.7 (1969)), but the doctrine of mootness is substantially the same for either. *Compare Tung-Sol*

Electric, Inc., 63 F.T.C. 632 (1963) with *Walling* v. *Helmerick & Payne, Inc.*, 323 U.S. 37 (1944).

The Supreme Court has ruled upon the concept of mootness in the context of a Section 8 case:

> Both sides agree to the abstract proposition that voluntary cessation of allegedly illegal conduct does not deprive the tribunal of power to hear and determine the case, *i.e.*, does not make the case moot. A controversy may remain to be settled in such circumstances, *e.g.*, a dispute over the legality of the challenged practices. The defendant is free to return to his old ways. This, together with a public interest in having the legality of the practice settled, militates against a mootness conclusion. For to say that the case has become moot means that the defendant is entitled to a dismissal as a matter of right. The courts have rightly refused to grant defendants such a powerful weapon against public law enforcement.
>
> The case may nevertheless be moot if the defendant can demonstrate that "there is no reasonable expectation that the wrong will be repeated." The burden is a heavy one. Here the defendants told the court that the interlocks no longer existed and disclaimed any intention to revive them. Such a profession does not suffice to make a case moot although it is one of the factors to be considered in determining the appropriateness of granting an injunction against the now-discontinued acts. *United States* v. *W.T. Grant Co.*, 345 U.S. 629, 632–33 (1952) (footnotes and citations omitted).

[32] A-M has entered into a consent agreement with the Commission which should eliminate, for that firm, further Section 8 difficulties. Mr. Shepard, by contrast, can continue to sit on TRW's Board of Directors for seven more years. Mr. Shepard's reputation for business acumen makes it likely that his services will be solicited by other firms and that other improper-interlock questions could arise. *See United States* v. *Trans-Missouri Freight Ass'n,* 166 U.S. 290 (1897). In my view, respondents have not convincingly met the heavy burden demanded of them by *W.T. Grant.* Respondents' reliance upon *United States* v. *Cleveland Trust Co.,* 392 F. Supp. 699 (N.D. Ohio 1974) is misplaced as they more closely resemble the position of defendant Cleveland Trust, as to whom the proceedings were not moot. Pneumo-Dynamics Corporation, another defendant there had effectively eliminated the means as well as the motive for violating Section 8. Similarly, *Paramount Pictures Corp.* v. *Baldwin-Montrose Chemical Co., Inc.,* 1966 Trade Cases ¶ 71,678 (S.D.N.Y. 1966), is of no help to respondents because the defendant there also had rid itself of the means for violating Section 8.

The Provisions of Section 8 of the Clayton Act

A reading of those parts of Clayton 8 applicable to the interlock between TRW and A-M through Mr. Shepard shows that four criteria must be met before its provisions apply. These are:

(1) One of the interlocked corporations must have capital surplus and undivided profits aggregating more than one million dollars;

(2) Each of the interlocked corporations must be engaged in interstate commerce;

(3) Neither of the corporations may be a bank, banking association, savings bank, trust company or common carrier; and

(4) The corporations, by virtue of their business and location of operation, must be competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the federal antitrust laws. *See generally* Wilson, *Unlocking Interlocks: The On-Again Off-Again Saga of Section 8 of the Clayton Act,* 45 ANTITRUST L.J. 324–25 (1976).

[33] Here each corporate respondent admitted that it met the million dollar requirement and that it was engaged in commerce as defined by Section 1 of the Clayton Act. Neither corporate respondent asserted that it is a bank, banking association, savings bank, trust company or common carrier. (Note: The Federal Trade Commission has challenged, under Section 5 of the Federal Trade Commission Act, an interlock between a savings and loan association and a bank. *Perpetual Federal Savings and Loan Association,* Dkt. 9083 [90 F.T.C. 608] (FTC Initial Decision, March 28, 1977). The initial decision by FTC Administrative Law Judge Timony holds that the interlocks challenged violated Section 5 of the FTCA. *Slip op.* at 41. That decision is on appeal to the Commission.)

Both respondent TRW and respondent Horace Shepard, as well as former respondent A-M, deny that TRW and A-M were competitors during the critical period (Answer of TRW, ¶ 10; Answer of Horace Shepard, ¶ 10; Answer of A-M, ¶ 6). Thus, the crux of the matter to be resolved, insofar as the charges brought under Clayton 8 are concerned, is whether TRW and A-M were competitors during the critical period. Clayton 8 itself does not indicate who are competitors beyond reciting that the corporations' business and location of operation are factors to be considered. Since both TRW and A-M are large, nationally and internationally engaged firms doing business in many of the same geographic areas (Findings 2–3, 8–9), their activities are such that the location of operation language in Section 8 is clearly met. It is not so clear whether their business activities were such during the critical period as to make them competitors.

For Purposes of Section 8, TRW And A-M Were Competitors During the Critical Period

Neither the Clayton Act nor its legislative history defines "competitors." Judicial opinions and writings regarding Clayton 8 do not go into great detail about the meaning of this word. This, no doubt, is because Clayton 8 decisions are infrequent and the statutory requisite of "competitors" has usually been stipulated. [34]

Complaint counsel argue that a showing that two corporations are in a position to form any agreement to violate the antitrust laws makes them, for purposes of Section 8, competitors (CCB at 16). I do not agree. In *United States* v. *Crocker National Corp.,* 422 F. Supp. 686 (N.D. Cal. 1976), an argument similar to complaint counsel's was made. Judge Peckham, in rejecting the argument, stated that the anomalous result of so holding would be that vertically related companies—suppliers and buyers—are competitors. 422 F. Supp. at 703. If followed to its logical end, the argument suggests, contrary to fact, that all corporations compete. This, because any two corporations could agree to do something violative of any antitrust law, *e.g.,* agree as to prices or to limit production, each of which is a *per se* violation of the antitrust laws. *See* REPORT OF THE ATTORNEY GENERAL'S COMMITTEE TO STUDY THE ANTITRUST LAWS (1955) at 12.

Section 8 requires a finding of both a competitor relationship and the ability of those competitors to eliminate competition by agreement. The first and significant factual determination is whether the interlocked firms are or were competitors. Since *Sears, Roebuck* v. *United States,* 111 F. Supp. 614 (S.D.N.Y. 1953), Section 8 has been said to have a "per se character." Halverson, *Interlocking Directorates—Present Antitrust Enforcement Interest Placed in Proper Analytical Perspective,* 21 VILL. L. REV. 393, 398–99 (1976). Such statements are only partially correct. Section 8 operates in *per se* fashion only after the factual determination of a competitor relationship. Judge Weinfeld, in *Sears, Roebuck,* explained the reason for the controlling effect of a finding of a competitor relationship over the "so that," *i.e.,* hypothetical anticompetitive agreement, portion of Section 8:

> This conclusion [that a per se reading was to be given to the "so that" branch of the Clayton 8 competitors test] is compelled because of the futility of trying to decide whether a given hypothetical merger would violate the pertinent sections of the antitrust laws. . . . The government's position presents no such difficulty. To accept its workable per se test . . . permits the prohibitory features of § 8 to be administered with the full scope which the legislators must have contemplated. 111 F. Supp. at 617.

[35] Section 8 becomes concerned about potential anticompetitive

agreements only when competing firms with a common director are involved. Once facts are found sufficient to conclude that two firms in interstate commerce compete (the three other statutory requisites of Section 8 having been met), analysis shifts to Section 11, the Clayton Act's enforcement provision.

In *Crocker,* Judge Peckham also said that, for Section 8 cases, "[w]hether two corporations were, in fact, competitors was apparently to be determined according to the traditional tests of competition—common sales in the same product and geographic market. This is the import of the phrase 'by virtue of their business and location of operation.' " 422 F. Supp. at 703–04. Previous Clayton 8 decisions have found, in seeming conformity with *Crocker,* a substantial quantity of common sales. In *Sears, Roebuck,* Judge Weinfeld noted that Sears, Roebuck and Goodrich Tire and Rubber Company conceded that they were competitors "in the sale . . . at retail" in 97 communities and 31 states to a volume of $80,000,000 annually of such things as refrigerators, hardware, sporting goods, auto supplies, tires, radios, television sets and toys. 111 F. Supp. at 617, 620. The Federal Trade Commission's recent decision in *Kraftco Corporation,* 89 F.T.C. 46, reflects that Kraftco and SCM stipulated that they were competitors in various parts of the United States in the sale of margarine, edible oils and barbecue sauce to a total of some $83,000,000. 89 F.T.C. at 48. It is important, however, to note that in *Kraftco* and *Sears, Roebuck* the statutory requisite of "competitors" was either admitted or stipulated. No precedent has been found in which the presence of sales or a certain dollar amount of sales has been conclusive in arriving at a decision about whether two firms were Section 8 competitors.

In my view, *Crocker's* test for competitors is too restrictive, for it may be read to suggest that the existence of competition hinges upon "sales" having been made. There can, however, be intense competitive efforts by firms interested in making a sale without any or all of them succeeding in persuading the buyer to purchase. Nonetheless, this effort, even when no sale results, indicates a competitor relationship. **[36]** More in keeping with my own notion of the type of activity which ought to be seen as evidencing the existence of a competitive relationship is the opinion of Mr. Justice Stevens, then sitting on the United States Court of Appeals for the Seventh Circuit, in *Protectoseal Company* v. *Barancik,* 484 F.2d 585 (7th Cir. 1973). The *Protectoseal* opinion indicates that two corporations competed for the same business in selling safety containers, faucets, fittings and accessories for flammable liquids. In fact, the defendant so testified. 484 F.2d at 587. Justice Stevens concluded that the language of Section 8 "contemplates a horizontal market relationship between the companies, [which] implies that a market-wide analysis of competition is unnecessary." 484 F.2d at 589. In *Brown Shoe* v. *United States,* 370 U.S. 294 (1962), a Clayton 7 merger case, the United States Supreme Court said that: "[A]n economic arrangement between companies performing similar functions in the production or sale of comparable goods or services is characterized as 'horizontal'." 370 U.S. at 334. *Perpetual Federal Savings & Loan Association,* in focusing upon "rivalry" rather than "sale" to support a finding of competitors, further advances understanding of the horizontal competitors relationship. The ALJ, in *Perpetual,* found on the basis of a stipulation as well as evidence that the interlocked bank and savings and loan association competed "in attracting savings and making residential loans." *Slip op.* at 20.

This discussion has not finally clarified the question as to who are "competitors" beyond the elementary notion of a horizontal relationship marked by rivalry. I believe that the way to come to grips with the concept of competitors is to recollect what Section 8 sought to protect. *Sears, Roebuck,* in its summary of the legislative history of Clayton 8, found that Section 8 was enacted to preserve competitive relationships and, as such, was to be broadly construed. Judge Weinfeld wrote:

> . . . Interlocking directorships on rival corporations had been the instrumentality of defeating the purpose of the antitrust laws. They had tended to suppress competition or foster joint action against third party competitors. The continued potential threat to the competitive system resulting from these conflicting directorships was the evil aimed at. Viewed against this background, a fair reading of the legislative [37] debates leaves little room for doubt that, in its efforts to strengthen the antitrust laws, what Congress intended by § 8 was to nip in the bud incipient violations of the antitrust laws by removing the opportunity or temptation to such violations through interlocking directorates. 111 F.Supp. at 616.

In this light, the best view as to who competitors are, in a Section 8 context, can be seen in the classic definition of competition set forth in *United States* v. *Standard Oil of New Jersey,* 47 F.2d 288 (E.D. Mo. 1931), a Sherman Act merger decision in which Circuit Judge Stone wrote "competition is, in its very essence, a contest for trade." 47 F.2d at 297. To the same effect is language in *United States* v. *The Philadelphia National Bank,* 201 F. Supp. 384 (E.D. Pa. 1952), *rev.* 374 U.S. 321 (1963):

> . . . the Congress by use of the word "competition," intended to preserve free and open markets wherein the rivalry of the commercial firms, in the same line of endeavor, for the patronage of the common customer, would be demonstrated by a business atmosphere where free purchasers and free sellers, under no obligation to

sell, would enter into contracts of purchase and sales (or service contracts) because of the actual inducements offered, such as quality of product, terms, delivery and the many other factors which make for good business relations, having in mind the peculiar situations, facts and circumstances which govern the particular transactions between individuals in organizations. 201 F. Supp. at 352.

The foregoing decisions support the view that in looking for standards by which to judge two firms "competitors," the critical element is the "contest" or "rivalry" for trade but an attempt to restrict the concept of "rivals" or "competitors" to a fixed set of circumstances would be unwise. As the quotation from *Philadelphia National Bank* suggests, the facts which may warrant the conclusion of rivalry for trade are too numerous to catalogue. The manner in which corporations and businessmen compete will change over time, but the relationship of "competitors"—when firms or individuals find themselves in a contest for trade—is constant. It is the relationship, rather than the ever shifting chain of causal factors, which Section 8 seeks to preserve and foster. All of this notwithstanding, [38] it still is necessary to do more than replace the legal conclusion of "competitors" with the equally unhelpful tag of "rivals."

"Competitors" in Section 8 does not have to be defined by a narrow set of announced facts because there is a simple method of inquiry for arriving at this legal conclusion. A finding that firms are competitors, for the purposes of Section 8, is reachable by using a conjunctive approach. That is: (1) Does a buyer, at least initially in the purchasing process, perceive, with good cause (*e.g.*, he observes their advertising, salesman calls, displays at conventions, etc.) that the products or services of two firms are more or less equally suitable to his end use? and (2) Have the charged sellers oriented their marketing efforts toward that buyer? This method of inquiry does not focus exclusively upon consummated sales, but considers all activity in the contest for trade. By considering the question of "Who are competitors?" from both a buyer's and seller's perspective, allegedly illegally interlocked sellers are safeguarded from eccentric buyer perceptions. Further, Section 8 is not rigidified by application of inappropriate antitrust tests. This last point is well illustrated by attempts to apply the cross-elasticity of demand and product interchangeability tests to a Section 8 case (*see* Munyon, Tr. 1365–73). *See generally, United States* v. *duPont deNemours & Co.*, 351 U.S. 377 (1956); *Brown Shoe Co.* v. *United States*, 370 U.S. 294, 325–28 (1962); *see also*, R. Posner, *Economic Analysis of Law*, 121–24 (1972). These tests were developed in order to define product markets for Sherman Act and Clayton Act monopoly, trade restraint or merger cases. In such cases, the antitrust laws are concerned with arriving at an objective economic measure of competitive harm. Section 8 on the other hand is oriented toward preserving the competitive situation as well as instances of objective competition. We are guided by Mr. Justice White's warning that "[I]nterchangeability of use and cross-elasticity of demand are not to be used to obscure competition but to 'recognize competition where, in fact, competition exists.' " *United States* v. *Continental Can Co.,* 378 U.S. 441, 453 (1963). Cross-elasticity of demand and product interchangeability are of use in a Section 8 proceeding, but they must not become the beginning and end of factual inquiry. [39]

The conjunctive approach leaves open the meaning of terms such as "purchasing process," "end use" and "marketing efforts" for application to the facts of a particular case. This is desirable because sophisticated pieces of computer hardware designed for use by large, institutional buyers are sold in a very different manner from the loaf of bread found on the local grocery shelf or the golf balls in a pro shop. Section 8 must be flexible enough to preserve the competitor relationship whether sophisticated devices, specialized products or consumer goods are being marketed by the interlocked corporations.

The attempts by TRW and A-M to persuade common prospective users, purchasers and lessees to buy or rent equipment capable of performing substantially identical functions evidences the fact that they were competitors during the critical period (*e.g.,* Findings 43-47). The electronic funds transfer and credit validation equipment industry was in its infancy when the interlock existed. There is no extended history with which one can measure competition between A-M and TRW in this industry before the Shepard interlock. In fact, the AMCAT, one of the devices A-M offered to prospects during the period for use in electronic fund/credit transactions, which competed with TRW's 4103 terminal, was not ready for the marketplace until Mr. Shepard became a board member of A-M (Finding 35). This is ironic because a relative scarcity of fully developed off-the-shelf "hardware," available from these companies during the critical period but with products adaptable to similar end uses, could be the genesis of greater anti-competitive effects from a common director than would vigorous attempts to sell fully developed "hardware." This, because design and production were still flexible and much of the effort by producers of devices for use in the electronic funds transfer industry such as TRW and A-M was toward persuading potential users to modify their plans and objectives so that the devices the supplier offered would meet the purchaser's needs (*e.g,* Findings 40, 45). [40]

In order to support the charge that a Section 8 violation occurred, complaint counsel does not here allege and need not prove that anticompetitive effects ensued from the interlock. Section 8 is designed to protect the market from future problems as well as present ones, and a developing industry is a most appropriate focus for enforcement. No one can second guess as to the direction in which two interlocked companies would have invested in research and market development had there been no common director. As the court said in *Sears,* 111 F. Supp. at 620:

> . . . a director serving in a dual capacity might, if he felt the interests of an interlocking corporation so required, either initiate or support a course of action resulting in price fixing or division of territories or a combination of his competing corporations against a third competitive corporation. The fact that this has not happened up to the present does not mean that it may not happen hereafter.

The *De Minimis* Defense Does Not Apply To Section 8

There are some provisions in Commission orders and in other judicial precedents suggesting that the dollar volume of sales in competition, in terms of the overlap in sales or as a percentage of either of the interlocked corporations' total sales, is significant in determining whether Section 8 has been violated. For example, in *United Brands Company,* FTC Dkt. 9034 (reported as *Kane-Miller. Corp., et al.,* 88 F.T.C. 279), par. II, consent order dated September 1, 1976—only sales in excess of $1,000,000 trigger the prohibitory provisions. The same is true of 12 consent settlements in which the order focuses only on overlaps of $1,000,000. These 12 orders bind a group of firms in the energy industry, *i.e.,* FTC Dkts. C–2684 - 2695, TRR ¶ 20,876 (73–6 Transfer Binder), *e.g.,* C–2684, par. 11, 86 F.T.C. 196, 198. [41]

In *Paramount Pictures Corp.* v. *Baldwin-Montrose Chemical Co.,* 1966 Trade Cases ¶ 71,678 at 82,065 (S.D.N.Y. 1966), the court held that "*de minimis* competition is not encompassed by the proscription of § 8." And in *Sears, Roebuck,* 111 F. Supp. at 621, the following appears: "Surely the sales of $80,000,000 do not come within the *de minimis* principle."

Also in *Sears, Roebuck* the court did say: "[T]he vital distinction between § 7 and § 8, however is that the latter omits the § 7 test and promulgates its own substantiality standard in the form of the one million dollar size requirement." 111 F. Supp. at 619. To the same result is language in *Crocker National Corp.,* 422 F. Supp. at 703:

> The real purpose of the "so that" clause seems to have been the establishment of a *per se* rule that interlocking directorates among competing corporations (that otherwise meet the requirements of the fourth paragraph of Section 8) are illegal. . . . Thus, in

furtherance of this purpose [nipping incipient antitrust violations in the bud], Congress sought to avoid questions as to whether the competition which interlocking directorates could potentially restrain was substantial or *de minimus* [SIC].

To the same effect is a comment by Mr. Wilson: "Accordingly, since no actual restraint is required, Section 8 amounts to a *per se* prohibition of all corporate director interlocks meeting the four statutory requirements." 45 ANTITRUST L.J. at 325.

Recent expressions in Commission adjudicative decisions as to the present state of the law on this point reflect that a *de minimis* argument is not a defense to a charge that Section 8 has been violated, *e.g., Kraftco Corporation.* There the Commission accepted without comment the ALJ's observation that: "A strong argument can be made that there is no *de minimis* defense in a Section 8 case because the statute prohibits interlocks where the competitive relationship is such that elimination of competition by agreement would violate *any* of the provisions of *any* of the antitrust laws." 89 F.T.C. at 53, n. 17. [42]

Applicability of Section 5 of the Federal Trade Commission Act

The complaint charges that both Section 8 of the Clayton Act and Section 5(a)(1) of the Federal Trade Commission Act were violated by the TRW/A-M interlock (Complaint, ¶ 7).

The legislative history and judicial decisions on Section 5 support the view that Congress intended it to enlarge the scope of existing statutory law so that the Commission could *supplement* the statutes as it discerned a need. The Senate committee report on enactment of the Federal Trade Commission Act includes the following:

The Committee was of the opinion that it would be better to put a general provision condemning unfair competition than to attempt to define the numerous unfair practices, such as local price cutting, interlocking directorates, and holding companies intended to restrain substantial competition. S. Rep. No. 597, 63d Cong., 2d Sess. 13 (1914).

Judicial decisions established long ago that the Federal Trade Commission Act was passed in order to go beyond the proscriptions spelled out in the antitrust laws. *F.T.C.* v. *Beech-Nut Packing Co.,* 257 U.S. 441, 453 (1952). More recently, in a landmark case, the Supreme Court said that the FTC was established ". . . to hit [along with the courts] at every trade practice, then existing or thereafter contrived, which restrained competition or might lead to such restraint if not stopped in its incipient stages. . . . The Commission has jurisdiction to declare that conduct tending to restrain trade is an unfair method of competition even though the selfsame conduct may also violate the Sherman Act." *F.T.C.* v. *Cement Institute,* 333 U.S. 683, 693 (1948). [43]

It also is well established that FTCA 5 applies to acts and practices which violate the antitrust laws, regardless of whether the violation is in letter or in spirit. *F.T.C.* v. *Sperry & Hutchinson Co.,* 405 U.S. 233, 239-44 (1972); *F.T.C.* v. *Brown Shoe, supra,* 384 U.S. at 322; *F.T.C.* v. *Motion Picture Advertising Service Co.,* 344 U.S. 392, 394-95 (1953); *F.T.C.* v. *Keppel & Bro.,* 291 U.S. 304, 314 (1934).

The Commission has announced its intention to use the FTC Act to supplement the antitrust laws. One example of such an announcement is found in the Commission's August 12, 1976, Statement of Policy (3 TRR ¶ 4,587 at 6956) regarding the naming of individuals in corporate interlock complaints:

> While the reach of Section 8 of the Clayton Act to interlocks between banks and other corporations such as savings and loans may not be clear,[6] no similar express statutory provision is contained in Section 5 of the FTC Act. The Commission has cited Section 5 as an independent basis of liability in interlock cases.[7] (Note: Footnote 6 is a quote from that part of Section 8 applicable to banks; footnote 7 is a cite to the *Kraftco* decision.)

Certainly, the legislative history of the FTC Act shows that the Congress said quite clearly an interlocking directorate is an unfair trade practice. (*See* quote above on p. 42; ". . . the numerous unfair practices, such as local price cutting, *interlocking directorates,* and holding companies . . . .")

In the recent initial decision in the FTC Act Section 5 case, *Perpetual Federal Savings & Loan Association, supra,* (pp. 10-11, *slip opn.*) ALJ Timony noted that, with the exception of certain banking organizations and common carriers, Clayton 8 prohibits interlocking directors between large competing corporations and provides that interlocks between savings and loan associations and banks violate the *policy* of Section 8 against interlocks of competing firms and amount to *incipient violation* of the Sherman Act. (15 U.S.C. 1). He [44] concluded that ". . . such *violations of the central policy* of the antitrust laws clearly violate Section 5." This is in harmony with the very well established interpretation in the 1941 *Fashion Originator's Guild* v. *F.T.C.* case, 312 U.S. 457 at 463. There, the Supreme Court declared that if the defendant's "*purpose and practice* . . . runs counter to the public policy declared in the Sherman and Clayton Acts, the Federal Trade Commission has the power to suppress it as an unfair method of competition." (Emphasis added.)

Respondents argue that ". . . Complaint Counsel has neither alleged nor shown that Mr. Shepard's simultaneous service on A-M's and TRW's Boards had any impact whatsoever upon competition. Thus, the alleged actions of Respondents could not have been an unfair method of competition 'in or affecting commerce,' and Section 5 cannot apply" (RB, p. 11).

However, the *Sears, Roebuck & Co.* decision, *supra,* 111 F. Supp. at 621, makes clear that the government need not show anticompetitive effects to sustain a Clayton 8 violation. And in *Perpetual* the ALJ found that a Section 5 violation based on the practice prohibited by Clayton 8 needs no proof of injury to competition or consumers. The latest Commission dual Clayton 8 and FTCA 5 case, *Kraftco,* does not reach the question whether ". . . the substantive standard for judging an interlock may be different under Section 5 . . ." (footnote 26 to ALJ's Conclusions, 89 F.T.C. at 58, adopted by the Commission, 89 F.T.C. 69) but leaves no doubt that Section 5 applies.

With regard to respondent TRW, the situation here parallels *Kraftco* more than *Perpetual.* In *Perpetual,* questions were raised about the underlying policy and jurisdictional extent of Clayton 8. Here, the allegedly illegal interlock, when examined in the light of the evidence, is clearly covered by the provisions of Section 8 and, here, the jurisdictional requisites of the Section were admitted. In such a situation, in contrast to the Kraftco/SCM situation, there is no need to resort to FTCA 5 in order to effectuate the policy reflected by Clayton 8. Enforcement action predicated on Section 8, the statute enacted specifically to bring an end to prohibited interlocking directorates is adequate to accomplish the Congressional purpose. [45]

As recently as January 1977, in its *Kraftco* opinion, *supra,* 89 F.T.C. at 64, when it was addressing the question whether a corporate respondent should be placed under a cease and desist order when violation of both Clayton 8 and FTCA 5 had been charged, the Commission said: ". . . no better illustration of a practice offensive to the spirit and policy of the antitrust laws if not their letter can be imagined than the employment and retention by a corporation of a director whose presence on the board itself violates the law. Application of Section 5 in such a case does no more than effectuate the clear purpose of the Clayton Act." Even so, it is worthy of particular note that both the Supreme Court in *Fashion Originator's* and the Commission in *Kraftco* suggested that affirmative action was critical in their thinking as to whether a violation of Section 5 had occurred. Further, the Commission's language in *Kraftco* reflects that affirmative corporate action must be found in order to serve as the predicate for issuance of an order under Clayton 8. No such action has been found here. Before interlocked corporations should be placed under either a Clayton 8, or an FTCA 5 order grounded on Section 8, culpability, a history of illegal interlocks, hostility toward or great reluctance in taking steps to avoid improper interlocks, none of which has been evidenced here, but several of which were in *Kraftco* (89 F.T.C. At 55–58, 65), must be shown.

Corporate Liability for Violations of Section 8

Prior Commission decisions make it very clear that corporations may be held accountable for interlocking directorates which are found to be illegal. Thus, in *Kraftco, supra,* the Commission said that Section 11 of the Clayton Act provides that only corporations may divest stock and assets and rid themselves of directors "chosen contrary to the provisions of sections 7 and 8 of this [the Clayton] Act," 89 F.T.C. 46, 62 (1977). The Commission's position on this is not unlike its position regarding a parent corporation's responsibility for the illegal acts of its subsidiaries. ". . . [I]f the facts demonstrate even latent control," the parent may be held vicariously liable for its subsidiaries' acts. *Beneficial Corporation and Beneficial Management Corporation,* CCH [1973–76 Transfer Binder, TRR ¶ 20,959 at 20,812 (FTC 1975) [86 F.T.C. 119 at 159]. This view has support from the decision of the sixth circuit court of appeals in *P.F. Collier & Son Corp.* v. *F.T.C.* 427 F.2d 266, 270 (6th Cir. 1970). The court said: **[46]**

. . . [W]here a parent possesses latent power, through interlocking directorates, for example, to direct the policy of its subsidiary, where it knows of and tacitly approves the use by its subsidiary of deceptive practices in commerce, and where it fails to exercise its influence to curb illegal trade practices, active participation by it in the affairs of the subsidiary need not be proved to hold the parent vicariously responsible. Under these circumstances, complicity will be presumed.

Counsel for TRW point out that in *United States* v. *W. T. Grant, supra,* 345 U.S. at 634, the Supreme Court expressly reserved judgment on the question as to ". . . whether corporations may violate Section 8 or, for other reasons, be enjoined under the statute," n.9. (Counsel also point out that the question currently is on appeal in *SCM* v. *F.T.C.,* Case No. 77–4978 (2d Cir. 1977).) A different view is found in the comment in "Antitrust Questions and Answers," Edwin S. Rockefeller, BNA Books, 1974, at p. 5, re the order issued in *Sears, Roebuck, supra:*

The district judge directed the individual defendant to resign his directorship in one or the other of the two companies involved and directed the company chosen to accept his resignation, but the court turned down the Government's request for a broad injunction against future violations of Section 8, stating in an endorsement on the back of the judgment that such decree "should be granted only where there is evidence showing a persistent purpose to violate or commit recurrences of the condemned act."

A part of the text of the order directed to Sears Roebuck in that case is set forth in *United States* v. *Sears, Roebuck & Co.,* 165 F. Supp. 356 (D.C. S.D.N.Y. 1958) in connection with an interpretation requested of Judge Weinfeld. It shows clearly that Sears, the corporation was enjoined along with Mr. Weinberg, the illegally interlocked director, at 357 and 359. [47]

Other Defenses Put Forward

In addition to the defenses already addressed, respondents asserted several others (*see,* pp. 3–4, *supra,* RB, pp. 12 and 30). One was that the complaint does not state a claim upon which relief could be granted. A reference to 5 U.S.C. 555, "Adjudications," and to the charges made in the complaint, however, is sufficient to show that respondents clearly were charged in the manner prescribed for administrative proceedings and that the allegations raised questions as to whether respondents had violated Section 8 and Section 5. The following expresses the rule:

> There is no requirement that a complaint in an administrative proceeding enumerate precisely every event to which a hearing examiner may finally attach significance. The purpose of the administrative complaint is to give the responding party notice of the charges against him. *See* 1 Davis—in Administrative Law Treatise §§ 8.04–8.05 and cases cited therein. The complaint is adequate if "the one proceeded against be reasonably apprised of the issues in controversy, and any such notice is adequate in the absence of a showing that a party was misled." *Cella* v. *United States,* 208 F.2d 783, 789 (7th Cir. 1953), *cert. denied* 347 U.S. 1016, 74 S.Ct. 864, 98 L.Ed. 1138 (1954); *Swift & Co.* v. *United States,* 393 F.2d 247, 252 (7th Cir. 1968). As the Commission case against petitioners unfolded, there was a 'reasonable opportunity to know the claims of the opposing party and to meet them.' *Morgan* v. *United States,* 304 U.S. 1, 18, 58 S.Ct. 773, 776, 82 L.Ed. 1129 (1938); *Swift & Co.* v. *United States, supra,* 393 F.2d 247, 252. *L.G. Balfour Co. et al.* v. *F.T.C.,* 442 F.2d 1, 19 (7th Cir. 1971).

What Justice Brandeis said many years ago remains true:

> All that is requisite in a complaint before the commission is that there be a plain statement of the thing claimed to be wrong so that the respondent may be put upon his defense. Dissent in *F.T.C.* v. *Gratz,* 253 U.S. 421, 430 (1920).

[48] The view of Justice Brandeis later came to be the view of the majority. *F.T.C.* v. *Brown Shoe Co.,* 384 U.S. 316, 320–21 (1966).

With regard to the no-public-interest defense, that is a point on which the Commission has said many times that an ALJ possesses no authority. In deciding to issue a complaint, the Commission proper, per Section 5(b) of the FTC Act, makes the determination that it has "reason to believe" that the proceeding is "to the interest of the public." Complaint counsel validly cites the decision on an interlocutory appeal in *Exxon Corp.*, 83 F.T.C. 1759 (1974), as a precedent holding that the ALJ has no authority in this area of Commission proceedings. A very recent expression to the same effect was handed down by the Commission in *Herbert R. Gibson, Sr., et al.*, Dkt. 9016. on October 12, 1977 [90 F.T.C. 275].

Another defense was that one of the grace period provisos in Section 8 obviates a finding of a violation in this case because complaint counsel failed to prove that TRW and A-M were competitors on November 7, 1974, one year before Mr. Shepard left the board of A-M (RB, pp. 30–35). The provisos in the Section authorize, as I understand them, (1) continuance as an illegally interlocked director for one year from the date of the "disabling" event when elected at a time when the corporation did not meet the $1,000,000 requirement but did later (penultimate paragraph), or (2) a change in the affairs of the corporation "from whatsoever cause" destroyed his/her eligibility (last paragraph). Clearly, here the $1,000,000 criterion exists and the "from whatsoever cause" language does not obviate the basis for the proceeding because TRW and A-M were competitors when they first offered devices to perform functions for members of the electronics-funds-transfer/credit transactions industry (Findings 23, 28, 33–34, CX 171, CX 8).

Section 8 is not clear on the point and neither is the legislative history, but I do not agree with the position of counsel for TRW that the one year grace period runs from the date of the director's election for the year in which the "disabling" event occurs. Such a holding could force an interlocked director to leave a board with only a few days of grace if the disabling event occurred just at the end of his term of service. Rather, I believe that it was the intent of the Congress to have the grace period run for at least one year from the date the "disabling" event occurs. In any event, the statutorily provided grace period does not affect my conclusion that instant interlock violates Section 8. This, as mentioned above, because TRW and A-M were competitors of each other well before November 7, 1974. [49]

The Staff Assurance that Respondents Would Be Apprised Before a Recommendation for Complaint Was Forwarded to the Commission

Counsel for TRW argues that respondents were denied due process, equal protection under the law and that they were the victims of an abuse of the administrative process by the Commission. The specific arguments made are:

(1) The August 8, 1975, letter from the FTC staff in Cleveland, Ohio, apprising TRW of the investigation reflected that the staff had concluded from their "findings" to recommend issuance of a complaint; however, TRW had been unaware of the investigation (RB, p. 80).

(2) The Cleveland FTC staff persisted in its attitude even though Mr. Shepard informed them that prior to his having learned of the investigation he had decided to leave the board of A-M at the next election of directors (RB, p. 80) and did so seven (7) months before the complaint issued.

(3) The Cleveland FTC staff requested only three bits of information in a letter dated October 31, 1975, but on November 14, 1975, before TRW could furnish it, the staff forwarded a recommendation to FTC headquarters in Washington, D.C., that complaint should issue (RB, p. 81).

(4) At the conclusion of a meeting in Washington, D.C., on December 10, 1975, attended by staff members from the Commission's Cleveland Regional Office and Bureau of Competition and the Assistant Executive Director for Regional Operations, counsel for TRW learned of the opposition of the staff of the Bureau of Competition to the issuance of a complaint. He was told that he would be informed by the staff before they forwarded such a recommendation to the Commission so that attempts might be made to persuade Commissioners to vote against issuance (RB, p. 80). **[50]**

(5) TRW, in reliance on this assurance, took no further steps (RB, p. 86) and the next contact counsel for TRW had from Commission staff was a telephone call on June 25, 1976, informing him that issuance of a complaint had been voted by the Commission on June 17, 1976 (RB, p. 80).

(6) On July 15, 1976, counsel for TRW was informed that the Commission had (1) rejected a Motion for Reconsideration filed by him on July 9, 1976, (2) refused to accept an Assurance of Voluntary Compliance simultaneously filed, and (3) forwarded these documents to an unidentified ALJ (RB, p. 84).

(7) On July 7, 1976, its General Counsel (GC) advised the Commission to take the position, and "hoped it was soon" (*see* RX 55-A) that complaints are issued when its members (three in this instance) vote issuance even though the Commission's Rules do not specify what constitutes "issuance." (Note: The significance of this is that the Commission's Rules provide that all motions are to be sent

to and addressed to the ALJ (except those to disqualify him) when a proceeding is before him (§ 3.22); hence, if the complaint were "issued" when voted, all motions thereafter were to be handled by the ALJ rather than the Commission. The Commission apparently took the GC's advice and on July 13, 1977, rejected "Respondents' Motion for Reconsideration and Related Relief . . .," dated July 9, 1976.)

The arguments regarding the paucity of knowledge respondents had regarding the staff investigation, the regional office's inexorable decision to recommend issuance of a complaint and the limited information requested of respondents are a part of the internal workings of the Commission and warrant no additional comment. [51]

The abbreviated recital of other actions, however, clearly shows that a most embarrassing and regrettable series of events occurred which would lead to great frustration, anger and resentment. But from a legal standpoint the actions were not so egregious that respondents were denied due process, denied equal protection under the law or subjected to an abuse of process. In an administrative proceeding respondents' *right* is to have due notice as to (1) when and where a hearing will be held, as well as the nature of the hearing, (2) the legal authority and jurisdictional basis for the hearing, and (3) the matters of fact and law asserted. 5 U.S.C. 554(b). *Golden Grain Macaroni Company* v. *F.T.C.,* 472 F.2d 882, 885–86 (9th Cir. 1972), *cert. denied,* 412 U.S. 918 (1973).

Respondents have been accorded each of these rights, even though the road they have had to travel was a tortuous one. The complaint and the various interlocutory matters, the prehearing conferences and orders and the adjudicative hearings provided the information and afforded those things to which respondents were entitled as a matter of legal, due process, right.

No one can reasonably argue that the staff assurance was not a professional commitment which *should* have been fulfilled. But the fact that it was not kept does not warrant a holding that respondents were prejudiced in the legal sense so that dismissal of the complaint would be appropriate. The fact that persons (in the broadest sense of the word) under investigation by the FTC may seek to persuade an individual Commissioner as to what his attitude should be toward investigative results and the fact that the Commission as a collegial body recognizes that this occurs does not establish a right to make such a presentation. On page two of its "Order" in this matter dated October 13, 1976, 88 F.T.C. 544, the Commission said at 545:

Neither the Commission's rules nor its practice provide for precomplaint presentations to the Commission, except for consent orders. The staff cannot create such a right by agreement with a respondent. Each Commissioner, in the exercise of discretion, determines whether to afford proposed respondents an opportunity to be heard before voting whether to issue a complaint.

[52] Clearly, whether such a presentation will be permitted is *solely* within the discretion of each Commissioner. There is no Commission rule which authorizes such presentations. That no staff person can grant or deny such permission so that the Commission or a Commissioner is bound, in the absence of authorized, specifically delegated authority not present here, has been well established for many years. For example, "The United States is neither bound nor estopped by acts of its officers or agents in entering into an arrangement or agreement to do or cause to be done what the law does not sanction or permit," *Utah Power & Light Co.* v. *United States,* 243 U.S. 389, 409 (1917). If this is true of statutory law, it cannot be less so with regard to administrative procedures which an agency establishes. Of course, an agency must rigidly adhere to those procedural rules which it has established (*Pacific Molasses Co.* v. *F.T.C.,* 256 F.2d 386, 389 (5th Cir. 1966)), but there was no Commission rule providing for what counsel for respondents was seeking.

Although no decision precisely in point has been found, in *Double Eagle Lubricants, Inc., et al.* v. *F.T.C.,* 360 F.2d 268 (10th Cir. 1965), where the Commission did not agree with staff advice as to where a disclosure should appear on a can of rerefined (used) oil, the court said:

The Commission is charged with the protection of the public interest. No principle of equitable estoppel bars it from the performance of that duty because of mistaken action by its subordinates.[5] Citing in n.5 *P. Lorillard* v. *F.T.C.,* 186 F.2d 52, 55 (4th Cir. 1950), cf. *United States* v. *San Francisco,* 310 U.S. 16, 32 (1940), and *F.C.C.* v. *Pottsville Broadcasting Co.,* 309 U.S. 134, 145 (1940).

It is true, as counsel for TRW suggests, that the trend is toward an erosion of sovereign immunity and toward the view that an agency sometimes may be estopped, *i.e.,* bound by the acts of its employees. *See* 2 K. Davis, *Administrative Treatise,* Section 1701 *et seq.,* esp. pp. 541–44. The courts, however, have not gone so far that what the staff did and failed to do here would warrant dismissal of the complaint. Cases cited by counsel for TRW held the government to be estopped when property of the federal government or [53] business dealings with the government were involved rather than, as here, where the subject matter is enforcement of the antitrust laws. For example, the *Brandt* v. *Hickel* case which counsel cites, 427 F.2d 53 (9th Cir. 1970)

(RB, pp. 91–92), deals with an oil lease. In *United States* v. *Wharton,* 514 F.2d 406 (9th Cir. 1975), the Whartons had settled on land on which the government sought to prevent them from getting a patent under the Desert-Land Entry Act of 1877 after the Whartons had acted in accord with government employees' advice (now 43 U.S.C. 321, *et seq.*).

If, for example, the Commission proper had given Mr. Shepard a favorable advisory opinion per Commission Rule 1.3 as to the interlock challenged here and then issued a complaint without first allowing him to resign, the doctrine of estoppel no doubt would apply. But that example is quite different from what happened to respondents.

Thus, I do not agree with the arguments of counsel for TRW that the Commission failed to comply with its own rules in its refusal to meet with him or his clients or to entertain his motion for reconsideration (RB, pp. 95–106). First, as noted above, there is no "rule" that binds the Commission, or any of the Commissioners, to meet with persons investigated by the staff before a vote is taken to consider whether a complaint should issue. Whether such a meeting is held is completely discretionary with the Commission or Commissioner to whom an approach is made. *See* the "Order" cited *supra,* at 88 F.T.C. 544, 545. Contrary to what counsel argues, the net effect of the GC's advice was no more than to suggest that the rules be made clearer as to when a complaint issues. It was merely a clarification which did not affect respondents' substantive rights.

Further, before the adjudicative hearings began, ALJ Hanscom certified the matter to the Commission together with the various documents respondents provided him which had been designed to convince the Commissioners to be approached that the complaint should not issue. *See* "Certification to the Commission for a Limited Purpose of Respondents' Motion for Reconsideration and Related Relief and Various Other Motions and Related Papers," dated September 15, 1976. Thus, the Commission and its members had the benefit of the facts respondents said they wanted to present before the hearings began and could have taken the action counsel for TRW was seeking. [54] That the Commission chose not to does not derogate from the fact that the Commission had TRW's arguments submitted to it. Consequently, respondents were not prejudiced, deprived of due process, denied equal protection of the laws and were not the victims of an abuse of the administrative process. Respondents must make a case sufficiently strong to convince that there was such substantial prejudice that procedural due process was denied them. *Arthur Murray Studio of Washington, Inc.* v. *F.T.C.* 458 F.2d 622, 624 (5th Cir. 1972). Respondents have not made such a case.

The Need for an Order

Respondents' counsel argues that a prospective order is unnecessary to protect the public from any future recurrence of an illegal interlocking directorate on the part of Mr. Shepard. He contends that (RB, pp. 74–77): (1) The complaint does not allege the possibility of future violations; (2) Mr. Shepard has given assurances of future compliance with Section 8 with respect to A-M as well as all other corporations; (3) Mr. Shepard is 65 and will retire as Chief Executive Officer of TRW; and (4) Mr. Shepard had been off the A-M board nearly seven months before the complaint was served.

The threshold question that underlies the construction of a remedy is what kind of order, within the broad range of an equity court's remedial powers, would, in the particular circumstances, be most effective to "cure the ill effects of the illegal conduct and assure the public freedom from its continuance." *Ekco Products Co.,* 65 F.T.C. 1163 (1964), *affirmed,* 347 F.2d 745 (7th Cir. 1965).

In both the initial decision of the ALJ and the opinion of the Commission in *Kraftco, supra,* there is language that affirmative corporate action suggesting culpability as contrasted with indifference or passivity, was persuasive in reaching the determination that SCM, the corporation, should be held accountable. Thus, the initial decision there supported issuance of an order against SCM on the basis that the corporation either did or could have (1) *seated* interlocking directorates, (2) *reaped* the anticompetitive benefits, and (3) possibly *appointed* new interlocking [55] directors after each was discovered. 89 F.T.C. at 51. To the same effect, the Commission said that the corporation might *maintain* an interlocking directorate and, if detected, simply *replace* the ousted director with another interlocking board member *without fear* that detection would result in anything more than the director's resignation, 89 F.T.C. at 63.

In contrast, there is nothing in the record of this case to suggest that TRW played an active role in Mr. Shepard's becoming a director of A-M, that TRW was indifferent or even hostile to the Commission staff's concern over the interlock, that TRW has an extensive history of being involved in interlocked director questions, that TRW was even interested in or resisted the ending of Mr. Shepard's interlock, or that TRW was disinclined to take action to prevent the occurrence of illegal interlocks in the future. This lack of action by TRW in doing those things, which might lead to the adverse competitive consequences with which the Congress was concerned when Section

8 was enacted, persuades me that in this case the corporate respondent should not be placed under an order to cease and desist.

This case is very different from the situation obtaining in *SCM/Kraftco, supra,* (*see* 89 F.T.C. at 65) in that:(1) the end of the interlock had been decided upon by Mr. Shepard before the Commission staff pointed out its concern (Finding 68); (2) it was affected by Mr. Shepard without TRW involvement seven months before the complaint issued (Findings 15, 17, 68); (3) it was a technical infraction rather than a substantive one (Finding 16); and (4) the record contains impressive evidence as to TRW's steps to improve further its procedures for preventing improper interlocks (Finding 17). Consequently, issuance of an order running to TRW is not called for.

As noted above, once the elements of a Section 8 violation are met, as they have been here, attention shifts to Section 11 of the Clayton Act. Section 11's sweeping language makes it clear that it was drafted so that there would be an effective remedy for every Clayton Act violation, but this does not mean that all respondents charged must be the objects of an order if a violation is found. The problem is not the reach of available remedies, but the just exercise of the reach. The question simply stated is: given a violation of Section 8, what are the guidelines governing the application of Section 11's sanctions? [**56**]

Paragraph (b) of Section 11 empowers the Commission to issue an order to a corporation to ". . . rid itself of the directors chosen contrary to the provisions of section[s] 8 . . . ." In pertinent part, the Section also authorizes modification or the setting aside in whole or in part of an order issued when ". . . conditions of fact or of law have so changed as to require such action or if the public interest shall so require. . . ." If that post-order-issuance discretion exists, there is no mandate that an order *must* issue against TRW since neither the facts adduced in the trial nor the public interest warrant such. In the light of the evidence in the record, neither the language of Clayton 8, the circumstances, nor the public interest calls for the issuance of an order against TRW under either Clayton 8 or FTCA 5. As to the discretion of an administrative law judge to issue an order, see *Kraftco, supra,* 89 F.T.C. at 55–56.

The order attached has been issued against respondent Shepard because it is the best protection of the public against the recurrence of an illegal interlock involving Mr. Shepard. It is based on authority set forth in Clayton 8 and FTCA 5 simply because the violation of Section 8 by him also violated FTCA 5.

The order has not been imposed because of a fear that Mr. Shepard would otherwise seek out directorships which violate the antitrust laws. In the past, Mr. Shepard has been asked to participate in the directorship of many large corporations (Findings 19–22), because of his reputation for business acumen. He will, no doubt, be asked to sit on other boards or otherwise to assist other businesses in the future. Although Mr. Shepard will no longer be the Chief Executive Officer of TRW, he will probably remain on the board for several years. (Finding 13).

TRW is a diversified corporation as are many other large corporations; and there is, thus, the clear possibility that Mr. Shepard's simultaneous membership either on such boards of directors, or otherwise as an officer, employee, agent or representative of a business, would violate Clayton Section 8 or [57] FTCA Section 5. Now that one such illegal interlock has been proven by the government, it would not only be incumbent on Mr. Shepard voluntarily to make absolutely certain that this situation does not again occur, but there also should be a sanction, as this order is, which goes beyond Mr. Shepard's assurances. The foregoing notwithstanding, it would be disingenuous to say that consideration also was not given to omitting an order running to Mr. Shepard. On balance, however, it is my belief that the public interests calls for the imposition of the order appended.

As the Commission stated in *Kraftco,* 89 F.T.C. at 66: "[W]e think the violation is itself the best evidence of the possibility of future occurrences, and that the burden rests with respondent to demonstrate that violations will not recur before consideration may be given to omitting an order . . . ." Discontinuance or abandonment of the violation does not remove the need for an order. *Fedders Co.* v. *F.T.C.,* 529 F.2d 1398 (2d Cir. 1976) *cert. denied,* 429 U.S. 818. The mere voluntary assurance by respondent to comply with the law is not necessarily an adequate safeguard for the future. *Clinton Watch Co.* v. *F.T.C.,* 291 F.2d 838, 841 (7th Cir. 1961), *cert. denied,* 368 U.S. 952 (1962). Nor does the possibility that other proceedings could be started if he was found again to be the conduit effecting an illegal interlock demonstrate the absence of a danger of recurrence. Nowhere has Congress suggested that those found to have violated Clayton Section 8 may be allowed several "bites at the apple." [58]

I do not agree with respondents' contention that the complaint must allege the possibility of future occurrences to sustain a prospective order. Respondents were served with the notice order and the trier of fact can go beyond the order accompanying the complaint, sometimes called "fencing in" to fashion an appropriate order to forestall future occurrences of the same or like nature.

F.T.C. v. *National Lead Company,* 352 U.S. 419 (1957); *Jacob Siegel Co.* v. *F.T.C.* 327 U.S. 608 (1946).

Respondents have also averred, in substance, that the prospective order should not issue because of complaint counsel's "unclean hands" in this case. As discussed in the *Other Defenses* section above, complaint counsel's actions are not controlling in determining whether issuance of an order is warranted. It is my view that a need for an order has been shown.

Conclusions

The Federal Trade Commission has jurisdiction over the respondents and the subject matter of this proceeding.

These proceedings and the order issued hereby are to the interest of the public.

When these proceedings began, respondents TRW and A-M had, and continue to have, capital, surplus and individual profits aggregating more than $1,000,000.

When these proceedings began, respondents TRW and A-M were, and have continued to be, in commerce or their business affected commerce as those terms are defined in the Clayton and Federal Trade Commission Acts.

Respondents TRW and A-M were competitors of one another during the period January 1, 1973, through November 5, 1975, in the manufacture, sale or distribution of point of sale credit authorization equipment, teller operated bank transaction equipment and other such equipment used for credit validation, recording of deposits and withdrawals from financial institutions, and inventory record keeping. [59]

Respondent Horace A. Shepard was a member of the Boards of Directors of TRW and A-M throughout the critical period January 1, 1973 - November 5, 1975.

The membership of Mr. Shepard on the Boards of TRW and A-M during the critical period violated Section 8 of the Clayton Act and Section 5 of the Federal Trade Commission Act.

The order issued should be addressed only to Mr. Shepard. Such an order follows:

Order

I

It is ordered, That respondent Horace A. Shepard, shall forthwith cease and desist from serving, and in the future shall not serve, as a director, officer, employee, agent, or representative of any corporation or other form of business entity if he simultaneously serves as a director, officer, employee, agent or representative of any other corporation, or other form of business entity, if such corporations or other forms of business entities are, by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws. [60]

II

It is further ordered, That within thirty (30) days from the date on which this order is served upon him Mr. Shepard shall file with the Commission a written report setting forth the manner and form in which he has complied with this order.

Opinion of the Commission

By Clanton, *Commissioner:*

I. Background

On June 17, 1976, the Commission issued a complaint against respondents TRW, Inc., Addressograph-Multigraph Corporation ("A-M"), and Horace A. Shepard, charging them with violations of Section 8 of the Clayton Act, 15 U.S.C. 19 and Section 5 (a)(1) of the Federal Trade Commission Act, 15 U.S.C. 45(a)(1). The basis for the complaint was the simultaneous membership of Mr. Shepard on the Board of Directors of TRW and A-M from January 1, 1973, through November 6, 1975 (the "complaint period"). The complaint alleged that during this period of time the business of TRW and A-M "included, but was not limited to, the manufacture, sale and distribution in commerce of point-of-sale credit authorization equipment and teller-operated bank transaction equipment, and other such equipment used for credit validation, check cashing validation, recording of deposits and withdrawals from financial institutions, and inventory record keeping" (Complaint, Paragraph 5). [2]

Subsequent to the complaint, A-M negotiated a consent order [90 F.T.C. 144] with the Commission on August 11, 1977.[1] In his initial decision filed with the Commission on December 22, 1977, the administrative law judge ("ALJ") found that Mr. Shepard's member-

[1] The relevant portions of the consent order provide that A-M: (1) is prohibited from having interlocking directorates with competitors if the elimination of competition by agreement between them would constitute a violation of the antitrust laws; (2) is required to review and retain a list of each A-M director, stating the name, address and products of each corporation for which the director is a member of the Board of Directors or a nominee; and (3) is required to review and retain prior to each election of directors, for each member of its Board of Directors and nominees, a descriptive list of all products and services of other corporations on whose board the director or nominee serves or to which he or she is a nominee.

ship on the boards of TRW and A-M violated Section 8 of the Clayton Act and Section 5 of the Federal Trade Commission Act. However, the ALJ entered an order only against Mr. Shepard on the ground that "neither the language of Clayton 8, the circumstances, nor the public interest calls for the issuance of an order against TRW under either Clayton 8 or FTCA 5" (ID p. 56).[2] Both parties [3] have appealed, respondents from the imposition of an order against Horace Shepard and complaint counsel from the ALJ's failure to enter an order against TRW.

II. The Parties and Relevant Products

A. Horace A. Shepard

Horace Shepard joined TRW as Vice President and Assistant to the General Manager in 1951. He was first elected to the Board of Directors of TRW in 1957 and has served continuously since that date. While he retired as an officer from TRW on November 30, 1977, at the age of 65, he can continue to sit on TRW's Board until he is 72 (ID 13). He was initially elected to the A-M Board on March 20, 1971, and served on that Board until his resignation on November 6, 1975 (ID 14).

B. TRW, Inc.

TRW is a publicly held corporation with net sales and revenues of $2,585,683,000 and a net income of $263,903,000 in fiscal 1975 (ID 1,3). During the course of these proceedings TRW was engaged, *inter alia,* in the design, manufacture and sale of a variety of products for industry and government, including those products relevant to this proceeding, as well as performance of advanced systems engineering, research and technical services in electronics and computer based services (ID 2).

TRW offered essentially three relevant product lines during the complaint period: the System 4000/5000, the Validata service, and certain products manufactured by FDS/i, a company which was acquired by TRW in April 1974 (ID 4, 23-31).

[2] The following abbreviations will be used in this opinion.

ID	- Initial Decision finding number
ID p.	- Initial Decision page number
Tr.	- Transcript page number
CX	- Complaint Counsel's exhibit number
RX	- Respondents' exhibit number
RAB	- Respondents' appeal brief
CAB	- Complaint Counsel's appeal brief
R.Ans	- Respondents' answering brief
C.Ans	- Complaint Counsel's answering brief
RFF	- Respondents proposed findings of fact

The System 4000/5000 was a credit authorization terminal[3] designed for use and sold to department stores (4000) and financial and thrift institutions (5000). Although the System 4000 [4] was marketed apart from the System 5000, the two systems were otherwise identical and used a terminal identified by the numbers 4103. The 4103, which was approximately 9 inches by 7 inches (Tr. 1235), had no ability itself to communicate with a computer. Rather it was connected to a controller, which in turn was connected by a dedicated telephone line to the host computer. The controller was located in the department store and was connected to as many as 128 terminals within the store. The computer, on the other hand, was located at a central location such as the headquarters of the department store (ID 23, 24; Tr. 1235–1244).

The Validata was an information service offered by TRW. What was sold was not the equipment but rather "loss protection" by means of an on-line file of stolen airline tickets, bad credit cards from 15 different credit card issuers, and a bad check file. Validata was utilized by airlines, car rental agencies, hotels and motels (ID 26, 27; Tr. 1819; Tr. 1253–54). Unlike the System 4000/5000, the data base was not maintained by the users but rather by TRW itself (Tr. 1820–21).

The third group of equipment offered by TRW during the complaint period was that which was acquired from FDS/i in 1974, and which formed the basis for TRW's electronic funds transfer system ("EFTS").[4] The TT–115, which was similar to the 4103 terminal requiring the use of a controller and dedicated telephone line (Tr. 1837), was used in a point of sale location by Glendale Federal Savings and Loan (ID 29). As so used, it provided for the deposit and withdrawal of money from a plastic card account, and the transfer of funds from a plastic card account to a supermarket account. In addition, the plastic card could be used as an identification card to authorize a personal check to pay for groceries (Tr. 1834–35).

TRW also offered within this group of products the TT–116 and the TT–117. Distinctive about the TT–116 was the ability of a customer to insert a check into the terminal for validation. The TT–117 differed from the other two products in that it was designed to perform credit authorization, as well as the other functions of check

[3] Credit authorization is a system whereby a clerk or customer enters certain information into an electronic terminal from which it is communicated to a main computer. The main computer then determines, from the information it has stored, whether the transaction should be authorized or denied (Tr. 246).

[4] EFTS is an electronic system whereby the "electronic impulses substitute for paper checks to describe the credits and debits related to a financial transaction" (Tr. 1682); in other words, the deposit and withdrawal of funds is made from a bank account without the traditional processing of checks.

validation and electronic transfer of funds. However, neither the TT–116 nor the TT–117 was sold by TRW during the complaint period. TRW produced only prototype models of the TT–116 and foam board mock up models of the TT–117 (ID 30,31). [5]

C. Addressograph-Multigraph Corporation

A-M is also a publicly held corporation with fiscal 1975 net sales and revenues totalling $584,246,000 and net income for that year of $4,908,000 (ID 7, 9).

Between January 1973, and November 1975, the relevant products offered by A-M were the AMCAT I, the AMCAT IC and the AMCAT II (Tr. 1723–24). The AMCAT I, which was introduced in the spring of 1973 (Tr. 1710–11), was a credit authorization terminal originally designed to meet the needs of the oil companies for use in gas stations. It contained all the communication functions within itself, and therefore could be used in a stand alone environment hooked up directly to a dedicated telephone line (ID 32, 33). It was approximately 16 inches long and wide and 8–9 inches high (Tr. 1275). Because the AMCAT I was able to operate in a stand alone environment free from the need for a communicator, it was utilized in small retail establishments which extended credit through third parties such as American Express (ID 34).

The AMCAT IC was a variation of the AMCAT I allowing direct operation by a consumer and containing a check tray for purposes of check verification (Tr. 1727–28). The modifications were made in part at the request of Robert Creekmore of the First National Bank of Atlanta for use in its Honest Face Program (ID 35; Tr. 17–2;[5] Tr. 1728–30).

The AMCAT II was designed for out of the way service stations in which use of the dedicated telephone line would have been too expensive. As such the AMCAT II was meant to be used in conjunction with the regular telephone lines (ID 35; Tr. 1725–26).

There were two other variations of the AMCAT–the HALFCAT and MODCAT. Both products were smaller versions of the AMCAT, but neither ever got beyond foam board mock ups (ID 35).

While the AMCAT family of products was initially designed for credit authorization purposes, it was ultimately adapted for EFTS use. As such, it was sold during the complaint period to Buckeye Federal Savings and Loan (ID 51–53) and to California Federal Savings and Loan (ID 60). [6]

[5] The trial transcript has been paginated in three sets: pages 1 to 180; pages 1 to 115; and pages 1 to 2179. To avoid confusion, we have referred to the first set with a "1" after the page number and to the second set with a "2" after the page number. The third set of numbers is referred to only by the relevant page number.

III. Mootness

At the threshold we are confronted with respondents' argument that this case should be dismissed because the issues raised are now moot. Respondents rely on several factors in making this argument. They contend that Mr. Shepard had determined in late 1974 or early 1975 to resign from A-M's Board and that his resignation was effective November 6, 1975, seven months before the Complaint issued. They also assert that TRW has instituted relatively stringent procedures to insure that simultaneous directorships will not take place in the future with A-M or any other corporation. Finally, they rely on the fact that in January 1977, A-M determined to discontinue its AMCAT product line, and indeed sold that line in June 1977.

It is well settled that "voluntary cessation of allegedly illegal conduct does not deprive the tribunal of power to hear and determine the case, *i.e.*, does not make the case moot." *United States* v. *W. T. Grant Co.,* 345 U.S. 629, 632 (1953). *See, e.g., United States* v. *Concentrated Phosphate Export Ass'n, Inc.,* 393 U.S. 199, 203 (1968); *Rubbermaid, Inc.* v. *FTC,* 575 F.2d 1169, 1172 (6th Cir. 1978); *Carter Products, Inc.* v. *FTC,* 323 F.2d 523, 531 (5th Cir. 1963). There exist considerations of public policy in determining the legalities of the issues involved, as well as the fact that the respondent is always free to return to his old ways absent any form of legal restraint. *United States* v. *W.T. Grant,* 345 U.S. at 632.

Nevertheless, if the respondent can demonstrate that there is no "reasonable expectation" that the wrong will be repeated, the case may be moot. *Id.* at 633. Such a demonstration, however, demands more than simply cessation of the wrong and a disclaimer that it will not be repeated.[6] There must be some showing that the cessation or abandonment of the practice was undertaken in good faith. Additionally, and more importantly, the respondent must show that the "challenged practices have been surely stopped under circumstances which assure that there is no reasonable likelihood of resumption of said practices . . . thus rendering the issuance of an order unnecessary." *Tung-Sol Electric Inc.,* 63 F.T.C. 632, 645 (1963). [7]

The time of the cessation, although not dispositive, nevertheless bears on the issue of good faith. While Mr. Shepard resigned prior to issuance of the complaint, his resignation occurred only after he was notified that an investigation was underway. Furthermore, there is evidence to indicate that the FTC's investigation was precisely why he chose to resign from A-M's Board (ID 68). On the other hand,

[6] We note that frequently cessation or abandonment is used as a synonym for mootness. As *Grant* and other decisions make clear, however, such usage is inaccurate.

there is testimony, which the ALJ credited, that Dr. Reuben F. Mettler, then President of TRW, learned well in advance of the Commission's investigation that Mr. Shepard intended to resign from A-M's Board (Tr. 939).

But even if we were inclined to accept Mr. Shepard's explanation for leaving A-M's Board, that action is not dispositive. In the final analysis, the issue of mootness turns on whether there is a likelihood of resumption of the questioned practice, for "the main goal of the Commission is to protect the public against continued or future violations of the statutes it administers". *Tung-Sol,* 63 F.T.C. at 646.[7]

Here, Mr. Shepard was sworn, as have several officials of TRW, that he will not again sit on A-M's Board, and that TRW will not violate Section 8. But such assurances are simply not sufficient and do not meet the stringent and heavy burden imposed on respondents by *Grant.* While Mr. Shepard may not sit on A-M's Board, there is no assurance that he will not be in a position where he could violate Section 8 in the future by sitting on other Boards that are in competition with TRW. Indeed, respondents do not argue that Mr. Shepard will refrain from membership on any other Board, but rather that it is unlikely at his age that he will be asked (RAB 10).[8] [8]

Likewise, the TRW affidavits relating to the installation of company procedures to prevent Section 8 violations, as well as the sale of the AMCAT product line, are not dispositive. *Tung-Sol* clearly demonstrates that the likelihood of resumption must be measured against changed circumstances which make it essentially impossible for the illegal activity to be resumed. Thus, for example, in *Tung-Sol,* there had been a change in industrywide practices such that "there exist[ed] no overall competitive condition which might prompt or even make feasible a return by respondents to the former practices." 63 F.T.C. at 650.

Other cases have similarly emphasized that the circumstances surrounding the challenged practices must be changed in a way which makes it highly unlikely that they will be repeated. In *Carter Products, supra,* the reviewing court agreed that the case was not moot, and cited the Commission's determination that, "[T]here has been no showing of *unusual circumstances* which would indicate that entry of an order is unnecessary nor does it appear that there has been any *change in the competitive conditions* which may have

[7] While this issue is closely intertwined with that of ultimate relief, "the two concepts are analytically distinguishable and a court could find that a case is not moot and yet deny injunctive relief." *SCM Corp.* v. *FTC,* 565 F.2d 807, 812 (2d Cir. 1977).

[8] It is also worth noting that even at the time he was considering whether to resign from A-M's Board, Mr. Shepard had already been invited to become a member of Procter and Gamble's Board (Tr. 939).

influenced respondents to use advertising of the type under consideration." 323 F.2d at 531 (emphasis added). Discontinuance of the unlawful practices also proved insufficient to serve as a defense in *P.F. Collier & Son Corp.* v. *FTC*, 427 F.2d 261, 275 (6th Cir. 1970), where the practices were "capable of being perpetuated or resumed . . . ." And, as the Commission noted in *Coro, Inc.*, 63 F.T.C. 1164, 1200 (1963), the respondent had failed to show that its abandonment of the illegal practices was not "forced upon it by business and economic conditions . . . ." In so concluding, the Commission distinguished other cases where, due to "the *total and permanent* character of the abandonment, it was concluded that resumption, because it would be economically unprofitable, was highly improbable." *Id.* at 1199–1200 (emphasis added).

We are not presented with such a situation here. While TRW no doubt intends to continue its screening procedures, there is in fact nothing which would independently cause it to do so. A-M's sale of its AMCAT product line in 1977 may, at this time, eliminate the competitive overlap between the two firms as to credit authorization and EFTS products, but it by no means prevents TRW and Mr. Shepard from interlocking with other [9] firms in the same product area or other lines of business.[9] Moreover, the very ease with which interlocks may be undertaken and withdrawn only underscores the importance of requiring a stronger showing of changed circumstances than has been presented here.[10] In short, the proof offered by respondents fails to demonstrate with some degree of certainty that "violations cannot recur," *Rubbermaid, Inc., supra,* 575 F.2d at 1172. Thus, we reject respondents' mootness contention. [10]

IV. Competition

[9] In further support of their mootness argument, respondents cite *United States* v. *The Cleveland Trust Co.*, 392 F.Supp. 699 (N.D. Ohio 1974), where the court dismissed a Section 8 count on the ground that one of the interlocking firms, a non-defendant in the case, had gotten out of the relevant product line. The court's decision rested primarily on *Paramount Pictures Corp.* v. *Baldwin-Montrose Chemical Co., Inc.*, 1966 Trade Cases ¶71,678 (S.D.N.Y. 1966). There the court, in an alternative holding, concluded that for Section 8 relief to be granted "there must still exist a *present ability* to resume any competition which may have ceased." *Id.* at 82,065–66 (emphasis added). In *Paramount*, the defendant sold its stock interest in one of the competing companies, leading the court to hold that this sale, negotiations for which had begun in good faith before issuance of the complaint, would be sufficient to warrant dismissal of the Section 8 charge. Here, TRW has not withdrawn from the credit authorization or EFTS business. A-M's exit only reduces one of undoubtedly many other possibilities for interlocks in this industry. TRW, as well as Mr. Shepard, clearly has a "present ability" to engage in similar interlocks in the future, even though A-M may not. To the extent *Cleveland Trust* suggests a different conclusion, we respectfully decline to follow it.

Moreover, even complete withdrawal by an interlocking firm from the competitive product lines might not justify declaring the case moot or refusing to issue an order. Additional evidence suggesting the possibility of future law violations, albeit in other product markets, could very well call for some form of prospective relief.

[10] Complaint counsel also contend that two prior Section 8 matters involving TRW and Mr. Shepard further undercut respondents' argument that violations are not likely to recur. (C. Ans 9; *see also* ID 19, 21). While these incidents are of limited evidential value, inasmuch as there was no adjudication of liability, they do illustrate the shortcomings of relying too heavily on discontinuance, which can be effected with relative dispatch, as a means of ensuring future compliance with Section 8.

Respondents next argue that A-M and TRW were not competitors during the complaint period, and thus, that Mr. Shepard's positions on both Boards did not violate Section 8. It is, of course, true that Section 8 requires that the allegedly interlocked corporations "are or shall have been theretofore by virtue of their business and location of operation, competitors so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws."

Though the issue of competition is central to a Section 8 case, in previous litigation under this section the parties have generally stipulated to the existence of competition.[11] That issue, however, is squarely before us here. Respondents contend that the appropriate tests for determining competition are whether there is (1) cross-elasticity of demand between the products or (2) reasonable interchangeability of use (RAB 27). By these measures, it is asserted, TRW's and A-M's products are not price sensitive nor are they sold to the same customers.

Complaint counsel, on the other hand, urge a more expansive interpretation of the term "competitors" by focusing on the proviso in Section 8 which reads as follows:

> so that the elimination of competition by agreement between [the competitors] would constitute a violation of any of the provisions of any of the antitrust laws.

This language, it is argued, defines what is meant by "competitors" and encompasses any test of competition under the antitrust statutes. Put differently, the relevant issue, as framed by complaint counsel, is whether the interlocking firms can "form an agreement that would violate the antitrust laws under the rule of reason analysis as it was known to Congress in 1914 under the *Standard Oil* decision" (CAB 33). [11]

The difficulty with complaint counsel's formulation is that it proves too much. As the ALJ noted, virtually any two corporations can fashion some kind of agreement which could violate the antitrust laws (ID p.34). It is not entirely clear what complaint counsel have in mind. If they mean that any competitive relationship may be reached by the statute—whether horizontal, vertical or potential—it seems fairly well settled that Section 8 applies only to firms which are horizontal competitors.[12] If, on the other hand,

[11] Although there was apparently no such stipulation in *Paramount Pictures*, the court gave only summary treatment to the issue of competition.

[12] *Protectoseal Co.* v. *Barancik*, 484 F.2d 585, 589 (7th Cir. 1973); *United States* v. *Crocker National Corp.*, 422 F.Supp. 686, 703-04 (N.D. Cal. 1976). *See also* Federal Trade Commission Report on Interlocking Directorates (1951). Of course, Section 5 of the FTC Act may reach interlocks involving firms in a buyer/seller relationship or between potential competitors, an issue we do not address here.

complaint counsel merely intend to suggest the approach for determining whether TRW and A-M are, in fact, competitors on a horizontal level, their interpretation of the Section 8 proviso provides little guidance. Since the case was brought and tried on a horizontal theory, we shift the focus of our inquiry to the criteria for assessing whether such a relationship existed.

In our view, a finding that two firms are competitors must be grounded on economic considerations. It is not enough to place undue focus on such vague, conclusory terms as "contest" or "rivalry" for trade, characterizations which are emphasized by both complaint counsel and the ALJ. While it is not inaccurate to describe competition broadly in this fashion, it does not materially advance the inquiry.

In judging whether competition exists, we believe it is appropriate to draw by analogy on concepts applied under Section 7 of the Clayton Act, 15 U.S.C. 18, and Section 2 of the Sherman Act, 15 U.S.C. 2, in defining a relevant product market. This approach is consistent with the language in Section 8 that corporations are competitors "by virtue of their business and location of operation." At the same time, it is clear that we need not get bogged down in a marketwide analysis, *Protectoseal Co.* v. *Barancik,* 484 F.2d 585, 589 (7th Cir. 1973), which requires the kind of product market definition that would be called for in a merger or monopolization case. [12]

As respondents point out, evidence of cross-elasticity of demand or product interchangeability is highly relevant in defining competition and drawing the outer parameters of appropriate product markets in other antitrust contexts. *Brown Shoe Co.* v. *United States,* 370 U.S. 294 (1962); *United States* v. *E. I. duPont de Nemours & Co.,* 351 U.S. 377 (1956). Nevertheless, the Supreme Court has cautioned that these criteria should not be used "to obscure competition but to recognize competition where, in fact, competition exists." *United States* v. *Continental Can Co.,* 378 U.S. 441, 453 (1964) (citation omitted) (Section 7 Clayton Act case). That guidance is even more relevant in a Section 8 proceeding where the market interaction of all competitive products, including those produced by the interlocking companies, will not be fully explored. Within this framework we turn to the facts of this case.

As was noted at the outset, both TRW and A-M manufactured, distributed and sold equipment used for credit authorization purposes.[13] Likewise, both manufactured and sold equipment used for the

[13] TRW's products were the System 4000/5000 and the Validata service, while A-M's products were the AMCAT line of goods.

electronic transfer of funds.[14] Nevertheless, TRW argues that because the equipment was purchased by different types of users and functioned in different ways they were not competitive products.[15]

There is no dispute that the products of both TRW and A-M accomplished essentially the same thing. The dispute is only as to the significance of "for whom" and "how." Thus, TRW argues that its System 4000/5000 was designed to work in a clustered environment (*i.e.*, large retail stores or other businesses with multiple check out stands) and in fact was at its economical peak when so placed (RAB 34-35). Nevertheless, the Heritage Bank Corporation in Chicago, Ill., placed its TRW credit authorization terminals in retail establishments in which there were no [13] more than 5-7 terminals (Tr. 94-2). Additionally, there was testimony that TRW's Validata Service, which utilized the same terminal as the System 4000/5000, was used by car rental agencies in off-airport premises in which only one or two terminals were used (Tr. 250; ID 18, 21-22).

TRW also argues that the various characteristics of the two products are so substantially different as to make them clearly distinct. However, the fact that TRW's 4103 did not have a card reading device could be overcome by ordering a separate piece of equipment from a different manufacturer. Indeed, Donald Kovar testified that the TT-115 sold to Glendale Federal contained a separately manufactured card reader (Tr. 1265-66).

Both TRW and A-M vied for the business of the same purchasers. There is more than ample testimony to reflect the fact that requests for information went out to, and initial contacts were made with, both companies by the same potential purchasers. Mr. Creekmore of the First National Bank in Atlanta ("FNBA") testified that he initially contacted 37 electronic terminal vendors, including TRW and A-M (ID 43). Mr. Wolfson testified that Metroteller, a subsidiary of Erie County Savings and Loan, also contacted both TRW and A-M (ID 48).[16] Furthermore, at a more serious level of bidding, both TRW and A-M would respond. Credit Systems, Inc. ("CSI"), for example, received responses to bids for quotations from both A-M and TRW (ID 56).

Beyond these discussions, both TRW and A-M would attempt to

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[14] TRW sold its TT-115 to Glendale Federal Savings and Loan. A-M sold its AMCAT to California Federal Savings and Loan.

[15] While complaint counsel alleged four categories of competitive equipment, the record is silent as to inventory recordkeeping and reveals that A-M never manufactured or sold teller operated bank transaction equipment (Tr. 1880). We are therefore concerned only with point of sale credit authorization equipment, including credit validation and check cashing validation, and equipment used for the electronic withdrawal and deposit of funds from a financial institution, *i.e.*, EFTS.

[16] There was similar testimony from Buckeye Federal Savings and Loan (ID 52), California Federal Savings and Loan (ID 61), Bank of America (ID 62), and Wells Fargo Bank (ID 66).

convince purchasers that what was really needed was the kind of equipment manufactured by each company, respectively. In its response to Bank of America's request for information, TRW urged reconsideration by the Bank of some of its requirements (CX 244). Likewise, Mr. Creekmore testified that TRW continued to attempt to sell FNBA a terminal which was not customer operated despite FNBA's express desire for one which was customer operated (Tr. 66–2).

If attempts to convince were not effective, the next course of action would be to develop new products or modify existing ones. Mr. Sheldon Kaplan, who was employed by A-M during the relevant time period, testified that he would first try to persuade a potential purchaser to use what A-M had already developed. Only after that first step would he change his tactic to determine what A-M could develop or modify (Tr. 176). Development and modification were in fact used by A-M for FNBA's "Honest Face" program (the AMCAT 1-C) (ID 45), and by TRW to meet Glendale Federal's need (ID 39–40). [14]

Attempts by TRW and A-M to persuade, develop and modify are especially significant when it is remembered that both credit authorization and EFTS were infant industries during the complaint period (ID 36). In fact, in many states the use of EFTS was not even statutorily permitted (Tr. 213–14). Thus, the industry was characterized by many products which performed the same function but in different ways. This was matched by customers who, because of the newness of the industry, did not have a particular set of requirements in mind. There was, as Mr. Thomas C. Noel, President of ELCOM Industries put it, "no specific, one universal set of requirements" (Tr. 137–1).

In view of this situation, it is not surprising that evidence of cross-elasticity of demand or product interchangeability would be less conclusive than where the products are fungible, or the technology standardized. At this stage of market development, it is understandable that customer needs would be more individualized, with particular attention devoted to product features and less to price.

As a consequence, it could be expected that the products of the two companies would not be readily interchangeable for all purposes. Yet, the adaptive responses of the firms to new demands suggest the kind of competitive response that is likely where a common market exists, even though the contours of that market may not be drawn with great precision. Moreover, despite the fact that for some uses the products may nct have been close substitutes (*e.g.,* large department stores vs. gasoline service stations), the evidence indicates that the systems were in much more direct competitive confrontation in other situations.

Perhaps the best illustration of the firms' ability to meet similar customer needs is found in the use of EFTS terminals in California supermarkets. Both Glendale Federal Savings and Loan and California Federal Savings and Loan decided to place EFTS terminals in Los Angeles supermarkets to allow the deposit and withdrawal of funds from customer accounts (ID 38, 60). While Glendale used the TRW TT–115 (ID 40), California Federal used the AMCAT I (ID 60). Glendale's TT–115 was small enough to fit into the check-out stand and utilized a personal identification number (PIN) pad. The AMCAT I had neither of these features (ID 39). Nevertheless, both terminals performed the same functions in the same type of retail environment. [15]

Furthermore, in response to Glendale's specifications, which included a magnetic card reader as well as a keyboard and digital display, A-M showed Glendale its MODCAT. While this terminal appeared to fit all of Glendale's needs, it was offered only after Glendale had already contracted with TRW for purchase of the TT–115 (ID 41).

That the market here does not reflect the tidiness that respondents or their expert witness, Dr. Paul Munyon, would like, does not negate the existence of effective competition between TRW and A-M. Though application of traditional tests for defining competition may lead to imperfect results in instances such as this one, where the market has not yet fully matured, we believe the record demonstrates that meaningful competition does exist and that it satisfies the standard set forth in Section 8. To the extent that the character of the competition, as opposed to its existence, has further significance, it should be considered in the context of fashioning appropriate relief.

V. One-Year Grace Period

Related to the issue of whether TRW and A-M were competitors is respondents' argument that paragraph 5 of Section 8[17] absolves Mr. Shepard of any liability under Section 8. Paragraph 5 provides for a

[17] This paragraph provides in pertinent part:

> When any person elected or chosen as a director . . . of any . . . corporation subject to the provisions of this Act is eligible at the time of his election or selection to act for such . . . corporation in such capacity his eligibility to act in such capacity shall not be affected and he shall not become or be deemed amenable to any of the provisions hereof by reason of any change in the affairs of such . . . corporation from whatsoever cause, whether specifically excepted by any of the provisions hereof or not, until the expiration of one year from the date of his election or employment.

one-year grace period from the date of a lawful election before liability attaches to an illegally interlocked director.

Respondents maintain that complaint counsel bears the burden of showing that Mr. Shepard was not eligible to be a director of A-M on November 7, 1974, the date of his last election and one year prior to his resignation (RAB 46). Complaint counsel have countered that there should be no exemption beyond the first election. Additionally, complaint counsel argue that the definition of "change in the affairs" should not include competition (C.Ans 38). [16]

In attempting to resolve the issue, the ALJ has interpreted paragraph 5 as being triggered by a "disabling" event rather than the date of election (ID p. 48). Without taking issue with the ALJ's interpretation, respondents alternatively argue that the ALJ erred by not finding such a disabling event (RAB 46).

We do not agree with the interpretation of either complaint counsel or the ALJ. Complaint counsel's position is based, in part, on the possible inconsistency that would result in subjecting directors (as well as officers and employees) who serve for terms in excess of one year to greater risk than directors who are elected (and reelected) for one-year terms. This stems from the fact that after one year a "change in the affairs" of a company would subject a director to immediate liability, whereas directors sitting for reelection each year presumably would have more time. Accordingly, complaint counsel urge that the most reasonable interpretation, which would apply fairly to everyone, would allow only one grace period, running from a director's or employee's initial election by the corporation or bank. While there may be some imperfections in the operation of this provision, the language of paragraph 5 is not limited to first-time elections. Moreover, the legislative history indicates that the author of the provision apparently felt that the one-year period generally conformed with the normal tenure of directors, at least bank directors. 51 Cong. Rec. 9603 (1914). In addition, there would appear to be no reason to assume new directors will be any less knowledgeable about a "change in the affairs" occurring after their election than other directors. That is particularly true where the change may be precipitated by action of the other company or companies involved in the interlock. Thus, we conclude that paragraph 5 applies to all elections of a director by the same corporation.

As for complaint counsel's second argument that a "change in the affairs" does not include the development of competition, neither the language of paragraph 5 nor its legislative history convinces us of the correctness of this interpretation. Paragraph 5 applies to a "change in the affairs . . . *from whatsoever cause* . . ." (emphasis added). And, the House debates indicate that the provision was added to address changes other than those relating to the size of the interlocking firms[18] which might affect the legality of an interlock (*Id.*). Certainly a change resulting in two firms becoming competitors for the first time is as significant as changes in the size of the asset or revenue base of a firm. Consequently, we believe paragraph 5 encompasses changes in the competitive status of interlocking firms that would trigger Section 8 liability. [17]

Finally, we find no basis for reading into the statute a requirement that the one-year period runs from the date of the "disabling" event, as suggested by the ALJ. Paragraph 5 explicitly provides that the grace period runs "until the expiration of one year from the date of [the director's] election . . ." The meaning of that language seems quite clear.

Nevertheless, notwithstanding our interpretation of paragraph 5, we do not find the one year exemption applicable in this instance. Implicit in our holding that TRW and A-M were competitors in the relevant product lines is that they were competitors on November 7, 1974. Indeed, TRW and A-M were competitors at least as early as May 1973, when A-M offered its AMCAT product line (RFF 47). Thus, as of the date of his last election to the A-M Board, Mr. Shepard was ineligible to sit as a director.

VI. *De Minimis* Defense

In conjunction with its argument on competition, respondents also contend that sales of the allegedly competing products were so small as to be *de minimis* and thus without the scope of Section 8.[19]

There is authority to suggest that such a defense is not appropriate to a Section 8 case, *United States* v. *Crocker National Corp.,* 422 F.Supp. 686, 703 (N.D. Cal. 1976); *United States* v. *Sears, Roebuck & Co.,* 111 F.Supp. 614, 619–21 (S.D.N.Y. 1953), since the statute is *per se* in nature and incorporates its own standard of substantiality. TRW and A-M have never disputed that they have "capital, surplus, and undivided profits aggregating more than $1,000,000" (ID 6, 11).

We need not resolve this issue, though, since we are not persuaded that respondents meet a *de minimis* standard however formulated. TRW's sales in the relevant product lines averaged $7 million annually during the period covered by the complaint (RX 62, RX

[18] Compare paragraph 4 of Section 8.

[19] Respondents in making their *de minimis* argument calculate TRW's sales data by excluding sales to department stores, airlines and car rental agencies. They justify this approach by claiming that A-M did not compete for this business (RAB 5–6). In view of our disposition of the competition issue, this approach is wholly inadequate.

62A, C.Ans 3), while A-M sales were about $1 million annually (RAB 5).[20] Although the sales of the products involved are relatively small in comparison to TRW's and A-M's overall revenues, such figures should not be viewed solely from the perspective of the two firm's operations. Consideration must also be given to the developing state of the technology and the fact that TRW's sale of its TT-115 EFTS system to Glendale Federal Savings and Loan was the largest EFTS project in the country at the time (Tr. 1688). Under these circumstances, we do not view the amount of commerce involved to be insignificant.

VII. Relief[21]

The ALJ, having found that Section 8 was violated,[22] entered an order against Mr. Shepard but not against TRW. Complaint counsel appeal the failure to enter an order against TRW, while respondents appeal the order against Mr. Shepard. We have determined that an order should issue against Mr. Shepard, but in a more limited fashion than proposed by the ALJ. We have also determined that under the circumstances, an order should issue against TRW. While we have wide latitude in fashioning a remedy, it must be reasonably related to the unlawful practices found to exist.[23]

A. Mr. Shepard

In deciding to issue an order against Mr. Shepard, we believe that Mr. Shepard's current status as a TRW director, together with his past membership on other boards, demonstrates a "cognizable danger" that a violation could occur again. [19]

The record contains evidence that Mr. Shepard has been a frequent member of various other boards. Indeed, as noted above, Mr. Shepard was approached by Procter and Gamble at the very time he was considering whether to resign from A-M. Under such circumstances, the likelihood of Section 8 violations is much greater than for an individual less sought after. Moreover, because TRW is a

[20] While the issue was not specifically referred to in *Protectoseal, supra*, we note that one of the corporations had competitive sales of only a million and a half dollars. 484 F.2d at 587.

[21] Although respondents have argued on appeal that broken commitments by the staff are of such a nature as to deny them due process and the right to a dismissal of this proceeding, we see no need to address this issue again. Our position was made clear in our order of October 13, 1976, 88 F.T.C. 544, and elaborated upon by the ALJ at p. 49 of the Initial Decision. Those decisions adequately deal with respondents' contentions.

[22] The ALJ also found violations of Section 5 of the FTC Act, as to both respondents, a decision with which we concur (ID p.59). Respondents have argued that in the absence of a Section 8 violation there is no independent basis for finding a Section 5 violation (RAB 46). In view of our disposition of respondents' liability under Section 8, we need not address this aspect of their appeal.

[23] *National Society of Professional Engineers* v. *United States*, 435 U.S. 679, 698 (1978); *FTC* v. *Colgate-Palmolive Co.*, 380 U.S. 374, 394-95 (1965); *FTC* v. *National Lead Co.*, 352 U.S. 419, 429 (1957); *FTC* v. *Ruberoid Co.*, 343 U.S. 470, 473 (1952).

large corporation with many products, the number of corporations which could be deemed competitive is also large. The combination of these factors persuades us that the public interest would be best served by issuance of an order against Mr. Shepard.

We are not inclined, however, to issue an order as broad as the one issued by the ALJ. The coverage of that order extends to Mr. Shepard's position as an "officer, employee, agent or representative of any corporation." Because the facts are not so egregious as to warrant such broad coverage, we require only that Mr. Shepard cease and desist from sitting on the Board of Directors of any corporation which competes with TRW.

This result is warranted by a combination of factors. In the first place, Mr. Shepard's age indicates that he may not be sought after by as many corporations as would otherwise approach a younger individual. The record does not indicate what the limiting age is for various corporations, but we suspect that TRW's age limit of 72 is not on the low side. At the time the appeal briefs were filed in 1978, Mr. Shepard was 65 years old and was eligible to remain on TRW's Board for seven more years.

We are further influenced by the fact that Mr. Shepard sought counsel before joining A-M's Board (ID 17). While such action does not absolve him of liability, it evidences some awareness of the concerns at stake.[24] Moreover, on at least one occasion, after having sought advice of counsel, Mr. Shepard declined an invitation to become a Director (ID 20). Both instances demonstrate at least some attempt by Mr. Shepard to comply with the mandate of Section 8. [20]

Lastly, we note that the nature of the violation is not as egregious as we have found in other instances. While such a distinction does not negate the need for an order, we regard it as mitigating the need for a broad fencing-in provision. Under the circumstances, we feel an order limited to his tenure on the Board of TRW should sufficiently sensitize Mr. Shepard to interlock problems that may arise if he chooses to sit on other boards in situations not covered by the order.

It should be made clear that our decision to limit the order against Mr. Shepard does not depend on any one factor, but rather on the combination of all three. In that context, this case presents a unique set of circumstances which we believe justifies a more limited form of relief.

[24] However, the fact that Mr. Shepard could rely, and apparently did rely, on Department of Justice statements during a 1971 investigation about competitive overlap between TRW and A-M, does not detract from the need for an order in this instance. Indeed, such reliance merely highlights the need to be constantly aware of changing products since the issue in the earlier investigation did not involve credit authorization or EFTS equipment.

B. TRW

Our determination to enter an order against TRW is based on different concerns.[25] The ALJ found, *inter alia,* that "there is nothing in the record of this case to suggest that TRW played an active role in Mr. Shepard's becoming a director of A-M" (ID p.55). Consequently, he determined that an order was inappropriate. We do not disagree with the ALJ's finding but rather with this conclusion. We think it is precisely TRW's failure to take action which is important. *Kraftco Corp.,* 89 F.T.C. 46, 65, *remanded on other grounds sub nom. SCM Corp.* v. *FTC,* 565 F.2d 807 (2d Cir. 1977). That TRW may have had no anticompetitive purpose in mind is beside the point. It is precisely to avoid such issues that Section 8 was enacted as a *per se* statute.

Mr. Shepard testified that he sought counsel from TRW (ID 17). It is therefore without question that TRW was aware of his membership on A-M's Board. While there may have been no competition between the two firms at the time Mr. Shepard was first elected to A-M's Board, competition arose over the course of time as new products were developed. It was therefore incumbent on TRW to monitor the legality of Mr. Shepard's membership. At a minimum, TRW should have evaluated Mr. Shepard's eligibilty each time he stood for election to TRW's Board. [21]

While TRW now has a screening process to avoid Section 8 problems, which followed on the heels of previous investigations, (Tr. 1026), we nevertheless believe that there is a "cognizable danger" that a Section 8 violation could occur again, and that TRW's screening process does not thoroughly insure against such future violations. Mr. Gorman testified that the screening process has been in effect since 1972 (*Id.*). Yet, Mr. Shepard's interlock with A-M went unnoticed until August, 1975, and then only after the Commission commenced its investigation.

In an attempt to avoid repetition of this very problem, we have structured the order to require each member or prospective member of TRW's Board to file with the corporation a written statement listing the products and/or services that are produced or sold by such other corporations on which the individual sits. In this way, TRW will have the benefit of an independently prepared list of products, which by its nature should be more thorough than a list prepared by TRW.[26] Furthermore, TRW will be prohibited from having on its Board any individual who fails to submit the required information.

[25] We do not understand TRW to argue that a corporation is not covered by Section 8. Indeed, such an argument has been recently rejected. *SCM Corp.* v. *FTC,* 565 F.2d 807, 811 (2d Cir. 1977).

[26] TRW currently prepares its own list from whatever sources it can find (Tr. 1031–35).

This requirement will remain in effect for a period of five years, at which time TRW will be free to utilize whatever other procedures it believes might be as effective.

Finally, we have limited the ban on interlocks with competing corporations to ten years. Normally a perpetual proscription is appropriate in view of the relatively clearcut statutory provisions and ease of compliance. Nevertheless, in view of mitigating factors, such as the nature of the violation and previous efforts to institute a screening procedure, even though inadequate, we find it unnecessary to bind respondent forever.

An appropriate order is attached.

Final Order

This matter having been heard by the Commission upon the cross-appeals of respondents and counsel supporting the complaint from the initial decision, and upon briefs and oral argument in support thereof and opposition thereto, and the Commission, for reasons stated in the accompanying opinion, having determined to deny the appeal as to respondents and grant the appeal as to counsel supporting the complaint:

It is ordered, That the findings of fact and initial decision of the administrative law judge be adopted insofar as not inconsistent with the findings of fact and conclusions of law contained in the accompanying opinion.

It is further ordered, That the following order to cease and desist be, and the same hereby is, entered:

Order

I. TRW, Inc.

The following definitions shall apply in this order:

"Subsidiary" of TRW means any corporation, 50 percent or more of the voting stock of which is owned or controlled, directly or indirectly, by TRW. [2]

"Parent" of TRW means any corporation which owns or controls, directly or indirectly, 50 percent or more of the voting stock of TRW.

"Sister" of TRW means any subsidiary of a parent of TRW.

1. *It is ordered,* That TRW, Inc., its successors and assigns, shall forthwith cease and desist from having, and in the future shall not have, on its board of directors any individual who either:

(a) serves as a director of Addressograph-Multigraph Corp., or any other corporation if TRW, Inc. and Addressograph-Multigraph

Corp., or such other corporation are, by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws; or

(b) fails to submit to TRW, Inc., any statement required by Paragraph Two of this order to be obtained by TRW, Inc.

The requirements of this paragraph shall be effective for a period of ten (10) years from the date of this order.

2. *It is further ordered,* That within thirty (30) days of the effective date of this order, and prior to each election of directors or prior to the solicitation of proxies for such election, whichever is earlier, TRW, Inc., shall obtain a written statement from each member of its board of directors (except directors whose terms expire at the next election and who are not standing for re-election) and from each nominee for a directorship (who is not then a director) showing:

(a) the name and home mailing address of each director or nominee; and

(b) the name and principal office mailing address of, and a listing of each product or service produced or sold by, each corporation which the director or nominee then serves as a director, or has been nominated to serve as a director at the time of the statement. [3]

The requirements of this paragraph shall not apply to elections of directors occurring after five years from the effective date of this order, nor shall directors or nominees be required to list products or services of subsidiaries, sisters, or parents of TRW, Inc.

Nothing in the paragraph shall be construed to relieve respondent of its obligation under Paragraph 1(a) hereto due to any error or omission contained in any written statement received pursuant to this paragraph.

3. *It is further ordered,* That within forty-five (45) days of the effective date of this order and annually for a period of ten (10) years hereafter, TRW, Inc., shall file with the Commission a written report setting forth in detail the manner and form in which it has complied with this order. Copies of the statements obtained pursuant to Paragraph Two of this order shall be submitted to the Commission as part of the reports of compliance required by this paragraph during the first five (5) years. Nothing in this paragraph shall relieve TRW of its obligation to comply with Paragraphs One and Four of this order once it is no longer required to submit reports of compliance to the Commission.

4. *It is further ordered,* That TRW, Inc., shall notify the Commission at least thirty (30) days prior to any change in the corporation such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of this order. The requirement of this paragraph shall be effective for a period of ten (10) years from the date of this order.

II. Horace A. Shepard

It is ordered, That Horace A. Shepard shall forthwith cease and desist from serving, and in the future shall not serve, as a director of any corporation or other form of business entity, if he simultaneously is serving as a director of TRW, Inc., if such corporation or other form of business entity and TRW, Inc., are, by virtue of their business and location of operation competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws.

IN THE MATTER OF

INDIANA DENTAL ASSOCIATION, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2957. Complaint, March 14, 1979 — Decision, March 14, 1979

This consent order, among other things, requires an Indianapolis, Ind. dental association and fourteen component societies to cease establishing or engaging in any policy, act or practice that may induce their members to refuse to submit data requested by third-party payers for benefit determinations; compel third-party payers to alter provisions of health care benefits programs; influence members to render other than independent judgments; or restrict consumers and third-party payers in their choice of dentists and/or dental consultants. Respondents are further required to mail a copy of the complaint and order to each of their members, together with a letter advising them that they are free to choose their own course of action in dealing with dental health care insurance plans.

Appearances

For the Commission: *Larry E. Gray.*

For the respondents: *Baker & Daniels, J.P. Barney* and *J.R. Genkins,* Indianapolis, Ind. and *P.C. Ward,* Washington, D.C., of counsel.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, (15 U.S.C. 41, *et seq.*), and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that the respondents named in the caption hereof have violated the provisions of Section 5 of the Federal Trade Commission Act and that a proceeding by it in respect thereof would be in the public interest, hereby issues this complaint, stating its charges as follows:

PARAGRAPH 1. The following definition shall apply in this complaint: "Third-party payer" or "payer" means any entity that provides a program of reimbursement for dental health care services to employees or members of any business organization, and any person, such as an independent claims adjuster, who provides evaluative services in connection with any such reimbursement program.

PAR. 2. Respondent Indiana Dental Association ("IDA") is an Indiana corporation with its principal office at 402 Jefferson Building, One Virginia Ave., Indianapolis, Indiana. IDA has approximately 2000 members, all of whom are licensed to practice dentistry in Indiana. IDA charters, and is divided into, geographic component societies. Membership in a component society is a condition of membership in IDA. The respondents alleged in Paragraphs Three through Sixteen comprise all the component societies of IDA. The component societies designate representatives who constitute IDA's House of Delegates, which is the governing body of IDA.

PAR. 3. Respondent First District Dental Society, an Indiana corporation, is a component society of IDA with its mailing address in care of Dr. Steven E. Dixon, 3700 Bellemeade Ave., Evansville, Indiana.

PAR. 4. Respondent Indianapolis District Dental Society, an Indiana corporation, is a component society of IDA with its principal office at the Illinois Building, 17 West Market St., Indianapolis, Indiana.

PAR. 5. Respondent Isaac Knapp Dental Society, an Indiana corporation, is a component society of IDA with its mailing address in care of Dr. Emory W. Bryan, Jr., 700 Indiana Bank Bldg., Ft. Wayne, Indiana.

PAR. 6. Respondent Western Indiana District Dental Society, an Indiana corporation, is a component society of IDA with its mailing address in care of Dr. Robert H. Michaels, 3120 Wabash Ave., West Terre Haute, Indiana.

PAR. 7. Respondent Ben Hur Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Michael A. McDonald, 1606 North Lebanon, Lebanon, Indiana.

PAR. 8. Respondent East Central Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Paul B. Risk, 610 S. Tillotson Ave., Muncie, Indiana.

PAR. 9. Respondent Eastern Indiana Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. John P. Backmeyer, 2519 East Main St., Richmond, Indiana.

PAR. 10. Respondent Greene District Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Keith M. Broshears, 290 A St., Linton, Indiana.

PAR. 11. Respondent North Central Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Dennis M. Miller, 3608 Pleasant St., South Bend, Indiana.

PAR. 12. Respondent Northwest Dental Society, a corporation, is a component society of IDA with its mailing address in care of Dr. Edward Young, 808 Madison St., LaPorte, Indiana.

PAR. 13. Respondent South Central Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Peter H. Leonard, 2739 Central Ave., Columbus, Indiana.

PAR. 14. Respondent South Eastern Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Elbert P. Combs, 411 Clifty Drive, Madison, Indiana.

PAR. 15. Respondent Wabash Valley Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. F. Wesley Peik, 3429 S. La Fontaine St., Kokomo, Indiana.

PAR. 16. Respondent West Central Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Lewis J. Urschel, 2204 Scott St., Lafayette, Indiana.

PAR. 17. Members of respondents are engaged in the business of providing dental health care services to patients for a fee and are paid for such services from the patients' personal funds and/or from funds provided under dental health care benefits programs. Except to the extent that competition has been restrained as herein alleged, members of respondents have been and are now in competition among themselves and with other dentists.

PAR. 18. Respondents are engaged in substantial part in representing the pecuniary interests of their members. By virtue of such activities, respondents are corporations organized for the profit of their members within the meaning of Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

PAR. 19. In 1976, total expenditures for dental health care services in the United States were approximately $8.6 billion. The annual rate of expenditures in Indiana is at least $150 million.

PAR. 20. In the course and conduct of their businesses, members of respondents:

(A) Receive substantial revenue from private third-party payers and from the Federal Government in payment for rendering dental health care services, which money flows across state lines;

(B) Receive and treat patients from states other than Indiana; and

(C) Utilize and prescribe substantial quantities of drugs, medicines, and other products which are shipped in interstate commerce,

as a result of which the acts and practices hereinbelow alleged are in or affect commerce within the meaning of the Federal Trade Commission Act, and respondents are subject to the jurisdiction of the Federal Trade Commission.

PAR. 21. A substantial portion of the population of Indiana is covered by dental health care benefits programs administered by third-party payers. Many of such programs include provisions for determination of benefits in advance of treatment ("predetermination") and limitation of coverage to the least expensive adequate course of treatment and require that radiographs ("X-rays") be submitted to aid in benefit determinations. The purpose of such provisions is to contain the cost of dental care. Their efficient utilization requires cooperation from treating dentists.

PAR. 22. For many years past, respondents and their members have formed agreements and engaged in acts, practices, and methods of competition having the purpose or effect of eliminating, preventing, or hindering competition among dentists with respect to cooperation by dentists with dental health care benefits programs containing predetermination and least expensive adequate course of treatment provisions.

PAR. 23. In the course of the conduct alleged in Paragraph Twenty-Two, respondents have requested, urged, and organized their members to refuse to submit X-rays to third-party payers or otherwise to cooperate with such payers by, *inter alia:*

(A) Promulgating, adopting, publishing, and distributing to members "Principles for Determining the Acceptability of Plans for the Group Purchase of Dental Care," a "Manual on Group Funded Dental Care Programs," and other guidelines for dealing with third-party payers, along with forms and information to facilitate adherence to such guidelines;

(B) Encouraging and inducing members to discontinue serving and/or to refuse to serve as dental consultants for third-party payers and to refuse to provide payers with other professional services such as, but not limited to, taking X-rays for use in benefit determination;

(C) Conducting meetings, workshops, and pledge campaigns among members to gain the agreement of individual members not to compete with other dentists in dealing with third-party payers;

(D) Urging dental organizations in other states to pursue courses of conduct similar to that hereinabove described; and

(E) Urging payers, purchasers, and beneficiaries of dental health care benefits plans to eliminate provisions of such plans that the respondents find unacceptable.

PAR. 24. As a result of the acts, practices and methods of competition alleged in Paragraphs Twenty-Two and Twenty-Three:

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(A) Competition among dentists in Indiana has been hindered, restrained, foreclosed, and frustrated;

(B) The cost of dental health care services in Indiana has been or may be stabilized or otherwise tampered with;

(C) Consumers have been or may be deprived of the benefits of third-party payers' cost-containing measures, including lower or potentially lower costs for dental health care services and dental health care benefits insurance;

(D) Consumers have been or may be denied the benefits of a second dentist's opinion as to the adequacy of proposed dental treatment; and

(E) Consumers have been limited in their opportunity to select dentists who cooperate with dental health care benefits programs.

PAR. 25. The aforesaid acts and practices constitute unfair methods of competition and unfair or deceptive acts or practices by respondents in violation of Section 5 of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and respondents having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of Section 5 of the Federal Trade Commission Act; and

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Indiana Dental Association ("IDA") is an Indiana corporation with its principal office at 402 Jefferson Building, One Virginia Ave., Indianapolis, Indiana. IDA charters, and is divided into, 14 geographic component societies, more particularly described below:

Respondent First District Dental Society, an Indiana corporation, is a component society of IDA with its mailing address in care of Dr. Steven E. Dixon, 3700 Bellemeade Ave., Evansville, Indiana.

Respondent Indianapolis District Dental Society, an Indiana corporation, is a component society of IDA with its principal office at the Illinois Building, 17 West Market St., Indianapolis, Indiana.

Respondent Isaac Knapp Dental Society, an Indiana corporation, is a component society of IDA with its mailing address in care of Dr. Emory W. Bryan, Jr., 700 Indiana Bank Building, Fort Wayne, Indiana.

Respondent Western Indiana District Dental Society, an Indiana corporation, is a component society of IDA with its mailing address in care of Dr. Robert H. Michaels, 3120 Wabash Ave., West Terre Haute, Indiana.

Respondent Ben Hur Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Michael A. McDonald, 1606 North Lebanon, Lebanon, Indiana.

Respondent East Central Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Paul B. Risk, 610 South Tillotson Ave., Muncie, Indiana.

Respondent Eastern Indiana Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. John P. Backmeyer, 2519 East Main St., Richmond, Indiana.

Respondent Greene District Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Keith M. Broshears, 290 A St., Linton, Indiana.

Respondent North Central Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Dennis M. Miller, 3608 Pleasant St., South Bend, Indiana.

Respondent Northwest Dental Society, an Indiana corporation, is a component society of IDA with its mailing address in care of Dr. Edward Young, 808 Madison St., LaPorte, Indiana.

Respondent South Central Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Peter H. Leonard, 2739 Central Ave., Columbus, Indiana.

Respondent South Eastern Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Elbert P. Combs, 411 Clifty Drive, Madison, Indiana.

Respondent Wabash Valley Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. F. Wesley Peik, 3429 South La Fontaine St., Kokomo, Indiana.

Respondent West Central Dental Society, an unincorporated association, is a component society of IDA with its mailing address in care of Dr. Lewis J. Urschel, 2204 Scott St., Lafayette, Indiana.

2. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and over the respondents, and the proceeding is in the public interest.

ORDER

I

It is ordered, That the following definition shall apply in this order: "Third-party payer" or "payer" means any entity that provides a program of reimbursement for dental health care services to employees or members of any business organization, and any person, such as an independent claims adjuster, who provides evaluative services in connection with any such reimbursement program.

II

It is further ordered, That respondents, their successors or assigns, and the officers, agents, representatives and employees of each of them, directly or through any subsidiary, division, or other device, shall cease and desist from engaging in any activity, course of conduct, practice, or policy that in whole or in part:

A. Requests, urges, recommends or suggests that dentists, or has the purpose or effect of requiring or organizing dentists to, (1) refuse to submit radiographs or such other pre-treatment and post-treatment reports, analyses and materials (except where post-treatment radiographs are not taken in the course of treatment and would expose the patient to unnecessary radiation) as third-party payers request for use in benefit determination or (2) refuse to deal in any particular way with any one or more third-party payers;

B. Compels or coerces any third-party payer to incorporate, delete or modify any provision in any existing or proposed dental health care benefits program;

C. Has the purpose of causing or inducing consumers to choose dentists who do not cooperate with third-party payers, or influencing, to any degree, consumers' choice of dentists based on the degree and/or manner of noncooperation between such dentists and any third-party payer or payers;

D. Has the purpose of compelling, coercing, or inducing any third-party payer to select particular dental consultants for reasons other than the expertise of such consultants; or

E. Has the purpose or effect of influencing any dental consultant to render any opinion other than that which reflects his independent expert judgment.

III

It is further ordered, That within thirty (30) days after this order becomes final, each respondent shall mail to each of its members a copy of the Commission's complaint and order in this matter, as well as a letter, in the form shown as "Appendix A" to this order, advising that respondents have abandoned all policies, guidelines and principles that request, urge, recommend or suggest that dentists, or have the purpose or effect of requiring or organizing dentists to, (1) refuse to submit radiographs or such other pre-treatment and post-treatment reports, analyses and materials (except where post-treatment radiographs are not taken in the course of treatment and would expose the patient to unnecessary radiation) as third-party payers request for use in benefit determination or (2) refuse to deal in any particular way with any one or more third-party payers. Furthermore, the letter shall further advise that dentists are free to choose to deal with any such programs and payers in such manner as they decide individually. In addition to the foregoing, each respondent shall mail a copy of the aforementioned complaint, order, and letter to every person who joins such respondent within five (5) years of the date of service of this order; *provided, however,* that mailing by the Indiana Dental Association will relieve the appropriate component society of the obligation of such mailing to a member of the Indiana Dental Association.

IV

It is further ordered, That, within sixty (60) days after service of this order, and annually on the anniversary date of the original report, for each of the five (5) years thereafter, each respondent shall individually file with the Commission a report in writing, setting forth in detail the manner and form in which it has complied with this order.

V

It is further ordered, That nothing in this order shall be construed to exempt any respondent from compliance with the antitrust laws or the Federal Trade Commission Act, and the fact that any activity is not prohibited by this order shall not bar a challenge to it under such laws and statute.

VI

It is further ordered, That each respondent shall notify the Commission at least thirty (30) days prior to any proposed change in it, such as dissolution, assignment, or sale resulting in the emergence of a successor corporation or association, or any other change in the corporation or association which may affect compliance obligations arising out of this order.

APPENDIX A

(Respondent's Letterhead)

Dear Doctor:

As you may be aware, the Federal Trade Commission (FTC) has been investigating certain activities of the Indiana Dental Association (IDA) and its component societies. IDA and its component societies have voluntarily entered into an agreement with the FTC which resulted in the issuance by the Commission on [date] of a complaint and the entry of a consent order which requires, in essence, that IDA and its component societies cease and desist from certain activities that are concerned with dental health care benefits programs and cooperation by dentists with the administrators of such programs. The order also requires that you be sent a copy of the complaint and order and this letter.

In accordance with the terms of the FTC's order, you are hereby notified that IDA and its component societies have abandoned all policies, guidelines and principles which request, urge, recommend or suggest that dentists, or have the purpose or effect of requiring or organizing dentists to, (1) refuse to submit radiographs or such other pre-treatment and post-treatment reports, analyses and materials (except where post-treatment radiographs are not taken in the course of treatment and would expose the patient to unnecessary radiation) as third-party payers request for use in benefit determination or (2) refuse to deal in any particular way with any one or more third-party payers. You are further notified that you are free to choose to deal with any such payers and programs in such manner as you decide individually.

Copies of the FTC's complaint and order are enclosed.

Sincerely,

____

President

Enclosures

IN THE MATTER OF

FORD MOTOR COMPANY, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9073. Complaint, Feb. 10, 1976 — Decision, March 29, 1979

This consent order, among other things, requires a Dearborn, Mich. manufacturer of motor vehicles, and the Ford Motor Credit Company to incorporate into specified documents a system for determining and accounting for all surpluses realized on repossessed vehicles resold by its dealers and to institute training programs designed to familiarize employees and dealers with their obligations in handling repossessions. Following such training, Ford is required to conduct a series of field audits to verify that dealers are calculating and paying surpluses correctly, and to submit timely compliance reports to the Commission. Additionally, respondents are required to inform dealers of their obligations to pay surpluses on past and future repossessions, and advise customers of their surplus and/or redemption rights, in the manner set forth in the order.

Appearances

For the Commission: *Bruce Carter, Barry Barnes, Dean A. Fournier* and *Daivd R. Pender.*

For the respondents: *George V. Burbach,* Dearborn, Mich. for Ford Motor Credit Co., *David R. Larrouy,* Dearborn, Mich. for Ford Motor Co., *Micheal Esler, Haessler, Stamer & Esler,* Portland, Ore. for Francis Ford, Inc. and *Carlton Harkrader* and *Thomas Brunner, Wald, Harkrader & Ross,* Washington, D.C. for Ford Motor Co. and Ford Motor Credit Co.

For the intervenor: *Glenn Mitchell, Stein, Mitchell & Mezines,* Washington, D.C.

COMPLAINT

The Federal Trade Commission, having reason to believe that Ford Motor Company, Ford Motor Credit Company and Francis Ford, Inc., corporations, have violated the provisions of the Federal Trade Commission Act, as amended, and that a proceeding in respect thereof would be in the public interest, hereby issues this complaint.

PARAGRAPH 1. *Respondents.* Respondent Ford Motor Company ("Ford") is a Delaware corporation with its office and principal place of business at The American Road, Dearborn, Michigan.

Respondent Ford Motor Credit Company ("Ford Motor Credit") is a Delaware corporation with its office and principal place of business at The American Road, Dearborn, Michigan. It is a wholly-owned subsidiary of Ford Motor Company.

Respondent Francis Ford, Inc. ("Francis Ford") is an Oregon corporation with its office and principal place of business at 509 S.E. Hawthorne Boulevard, Portland, Oregon.

Allegations stated below in the present tense include the past tense.

PAR. 2. *Respondents' Business.* Ford manufactures, distributes and sells motor vehicles, including automobiles and trucks. It also owns all or part of the voting stock of various retail dealers of its vehicles, whose business operations and policies it controls. It is responsible for the acts and practices of its wholly- or partially-owned dealers.

Wholly- or partially-owned as well as independent retail Ford dealers are referred to below as "Ford dealers."

Ford Motor Credit is a finance company which provides retail financing to customers of Ford dealers for their retail installment contract purchases of new and used motor vehicles. It also provides wholesale financing for inventories held by Ford dealers.

Francis Ford is a franchised Ford dealer selling new and used motor vehicles.

PAR. 3. *Commerce.* Each of respondents participates in some or all phases of the sale, distribution and repossession of motor vehicles, and in the transmission across state lines of contracts, monies, and other business papers related to the extension and enforcement of credit obligations. Respondents each maintain a substantial course of trade in motor vehicles and motor vehicle credit in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 4. *Retail Installment Contract Sales.* Francis Ford and most other Ford dealers arrange financing through Ford Motor Credit or other lenders for retail sales of motor vehicles to their customers. Most of the sales to be financed by Ford Motor Credit are executed on a printed "retail installment contract" form provided by Ford Motor Credit, naming the customer as buyer and the dealer as seller. This "retail installment contract" form indicates that the contract is to be assigned to Ford Motor Credit for value, that the buyer is to be indebted to the dealer or its assignee, and that the dealer or its assignee is to be a secured party holding security interest in the vehicle sold. In the event the buyer defaults, Ford Motor Credit and Francis Ford and other retail Ford dealers have also undertaken the obligation, by express or implied representations in their retail installment contracts, to account to the defaulting buyer for any surplus arising from the resale of repossessed collateral. This obligation is reaffirmed after default in notices sent to defaulting buyers by Ford Motor Credit. These representations have the tendency and capacity to lead buyers to a reasonable expectation that Ford Motor Credit will refund any surplus.

PAR. 5. *Statutory Duty to Account for Surplus.* The respective rights and duties of the defaulting buyer and secured party after repossession are defined by state commercial law, derived by almost every state from Article Nine of the Uniform Commercial Code, and the retail installment contract. State law requires the secured party, after repossessing and/or disposing of the collateral, to account to the defaulting buyer for any surplus of proceeds from the sale or disposition in excess of the amount needed to satisfy all secured indebtedness, reasonable expenses of retaking, holding, preparing for sale, selling, and the like, and allowable legal costs and fees.

PAR. 6. *Post-Default Procedures Determined by Master Agreement.* In instances where Ford Motor Credit as secured party declares a default, it usually repossesses or causes repossession of the vehicle. The procedures followed by Ford Motor Credit and the dealer after repossession are determined by a master agreement embodied in the "Ford Motor Credit Company Retail Plan," between Ford Motor Credit and the dealer, as well as by the terms of the assignment of each retail installment contract to Ford Motor Credit. Additional terms are spelled out in Ford Motor Credit's legal guides and operations manuals. A majority of the agreements executed between Ford Motor Credit and Ford dealers in the United States are repurchase or similar agreements (hereinafter "repurchase" agreements).

PAR. 7. *Repurchase Transfer and Payoff.* Pursuant to the agreements described in Paragraph Six, Ford Motor Credit in most instances returns the repossessed vehicle to the repurchase dealer and receives from the dealer a payoff, consisting of the unpaid balance of the retail installment contract adjusted by applicable charges and credits. The dealer then resells the vehicle to a third party.

PAR. 8. *Joint Liability.* Under applicable state law, a dealer who receives a transfer of collateral from a secured party pursuant to a repurchase agreement has a duty to properly dispose of the collateral and to account to the defaulting buyer for any surplus. Ford Motor Credit also is obligated to ensure that a proper disposition of the collateral is made and that a proper accounting for any surplus is given to the defaulting buyer. Ford Motor Credit shares this obligation jointly with the dealer because (1) it continues to be the secured party and continues to be a fiduciary with respect to the defaulting buyer's equity interest; (2) Ford Motor Credit, as assignor of the contractual duties of a secured party, continues to be liable for performance of those duties; (3) Ford Motor Credit has dictated, controlled and acted jointly with the repurchase dealer in executing relevant aspects of the credit transaction; and (4) Ford Motor Credit has made representations to buyers, as set forth in Paragraph Four, that these duties would be properly performed.

PAR. 9. *Failure to Account for Surpluses.* In a substantial number of instances Ford Motor Credit, Francis Ford, and other Ford repurchase dealers, have (1) failed to institute or follow correct procedures for determining the existence or amounts of surpluses realized from the sale of repossessed vehicles, (2) failed to disclose the existence of these surpluses to defaulting buyers, and (3) wrongfully retained such surpluses in violation of the defaulting buyers' statutory and contractual rights. The failure to identify and disclose surpluses has concealed their existence from these consumers and consequently few have asserted their rights under applicable state law. The failure to remit surpluses has deprived numerous consumers of substantial amounts of money rightfully theirs and has unjustly enriched Ford Motor Credit and its repurchase dealers. These practices are therefore unfair and deceptive.

PAR. 10. *Failure to Disclose Material Facts Concerning Redemption.* Ford Motor Credit and its repurchase dealers fail, in some instances, to inform defaulting buyers of facts necessary to their exercise of the right of redemption granted by state law, including but not limited to (1) the nature and duration of the right to redeem, and (2) the amount required to redeem. This failure to disclose material facts has the tendency and capacity to hinder defaulting buyers in exercising the right to redeem and is therefore an unfair and deceptive act or practice.

PAR. 11. *Owned Ford Dealers Using Non-Ford Motor Credit Financing.* A number of wholly- or partially-owned Ford dealers engage in the acts and practices ascribed to dealers in Paragraphs Nine and Ten, in instances where retail installment financing for their customers is obtained from finance institutions other than Ford Motor Credit. These acts and practices, for the reasons stated above, are unfair and deceptive.

PAR. 12. *Conclusion.* The acts and practices of respondents set forth in Paragraphs Nine, Ten, and Eleven are all to the prejudice and injury of the public and constitute unfair and deceptive acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.

Commissioner Nye dissented.

Decision and Order

The Commission having heretofore issued its complaint charging the respondents named in the caption hereof with violation of Section 5 of the Federal Trade Commission Act, as amended, and the respondents having been served with a copy of that complaint together with a proposed form of order; and

The respondents Ford Motor Company and Ford Motor Credit Company, their attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, admissions by these respondents as to the Commission's jurisdiction, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in the complaint, and waivers and other provisions in accordance with the Commission's Rules; and

The Commission having thereafter, in accordance with Section 3.25(c) of its Rules, withdrawn this matter from adjudication as to Ford Motor Company and Ford Motor Credit Company; and

The Commission having considered the matter and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed pursuant to Section 3.25(f) of its Rules, now in further conformity with the procedure prescribed in Section 3.25(f) of its Rules, the Commission hereby makes the following jurisdictional findings and enters the following order:

1. Respondent Ford Motor Company is a Delaware corporation with its office and principal place of business located at The American Road, Dearborn, Michigan.
2. Respondent Ford Motor Credit Company is a Delaware corporation with its office and principal place of business located at The American Road, Dearborn, Michigan.
3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding as to Ford Motor Company and Ford Motor Credit Company, and of these respondents, and the proceeding is in the public interest.

Order

I.

It is ordered, That for purposes of this order the following definitions shall apply:

A. "Ford respondents" means Ford Motor Company ("Ford") and Ford Motor Credit Company ("Ford Credit"), corporations. It shall not refer to Francis Ford, Inc. References to either or both of the Ford respondents shall include their successors, assignees, officers, agents, representatives and employees, as well as any corporations, subsidiaries, divisions or devices through which they act in the United States. *Provided, however,* that references to Ford shall not include Ford Credit and references to either or both of the Ford respondents shall not include dealerships.

B. "Vehicle" means a passenger car or a truck with a gross vehicle weight less than 26,000 pounds (11,794 kilograms).

C. "Dealership" or "dealer" means a corporation, partnership or proprietorship that is a Ford, Lincoln or Mercury vehicle dealership but excludes truck dealerships whose principal business is the sale of trucks with a gross vehicle weight more than 8,000 pounds (3,629 kilograms).

D. "Retail sale" means the installment credit sale of a vehicle, other than for purposes of resale, (*e.g.,* sale to dealers or wholesalers), lease or rental, to a purchaser who is not a fleet purchaser.

E. "Repurchase financing" means the financing of a retail sale subject to an agreement between a financing institution and a dealership (generally called a "repurchase," "recourse," or "guaranty" agreement) which provides that the dealership is obligated to pay off the outstanding obligation to the financing institution after receiving a transfer of the repossessed vehicle.

F. "Repurchase dealership" or "repurchase dealer" means a dealership that engages more than occasionally in repurchase financing transactions.

G. "Equity dealership" means a dealership in which Ford has a controlling equity interest, holds 50 percent or more of the voting stock, or is entitled to elect 50 percent or more of the board of directors.

H. "Liquidating dealership" means an equity dealership that has ceased or is in the process of ceasing normal operation of a dealership and whose business has been or is being wound up by Ford or under Ford's supervision. It shall not mean a dealership not previously an equity dealership whose assets come into the possession or control of either of the Ford respondents by virtue of default on or compromise of a debt obligation.

I. "Financing customer" means a purchaser of a vehicle from a dealership by means of a retail installment contract.

J. "Disposition" or "dispose" refers to a dealership's sale or lease of a repossessed vehicle previously sold by that dealership and returned to it by or for a financing institution pursuant to a repurchase agreement. Such sale or lease includes only transactions with an independent third party; *i.e.*, it does not include a sale or lease to the financing institution, the dealership or their representatives, or to a person or firm liable under a guaranty, endorsement, or repurchase agreement covering the repossessed vehicle. Disposition or dispose shall not refer to the repurchase of a repossessed vehicle by a dealership pursuant to a repurchase agreement, or refer to a sale subsequent to a judicial sale in Louisiana.

K. "Proceeds" means whatever is received upon disposition of the repossessed vehicle, but exclusive of sales taxes, services contracts or separately priced warranties.

L. "Allowable expenses" means only actual out-of-pocket expenses incurred as the result of a repossession. The expenses must be reasonable and directly resulting from the repossessing, holding, preparing for sale and reselling of the vehicle, and not otherwise reimbursed to the dealership. They are limited to the following charges (if allowable under applicable state law):

1. expenses paid to others, who are not employees of the dealership or of the financing institution that financed the vehicle, for repossessing, towing or transporting the vehicle;

2. filing fees, court costs, cost of bonds, fees paid to a sheriff or similar officer, and fees and expenses paid to an attorney who is not an employee of the dealership or the financing institution for obtaining possession of or title to the vehicle;

3. fees paid to others to obtain title to the vehicle, to obtain legally required inspection of the vehicle, or to register the vehicle;

4. expenses paid to others for storage (excluding a charge for storage at facilities operated by the dealership);

5. labor and associated parts and supplies furnished by the dealership for the repair, reconditioning or maintenance of the vehicle in preparation for resale, computed at dealer cost (as defined in the Initial Compliance Report) with appropriate adjustments for any insurance or warranty recovery;

6. amounts paid to others for labor and associated parts and supplies purchased for the repair, reconditioning or maintenance of the vehicle in preparation for resale;

7. sales commissions paid for actual participation in the sale of the particular vehicle, computed at a rate no higher than for a similar, nonrepossessed vehicle and excluding portions of commissions attributable to the selling of service contracts, separately priced warranties, financing or insurance;

8. expenses of advertisements that specifically mention the

particular vehicle, including a proportional share of any advertisement that also mentions other vehicles;

9. auctioneer expenses and fees paid; and

10. expenses for telephone calls and postage incurred in arranging for the repossession, holding, transportation, reconditioning and resale of the vehicle.

M. "Contract balance" means (1) the unpaid balance as of the date of repossession less applicable finance charge and insurance premium rebates deducted by the financing institution, plus (2) other charges authorized by contract or law and actually assessed prior to repossession.

N. "Surplus" means the excess of (1) the proceeds plus applicable insurance or warranty reimbursements received by the dealership or financing institution plus any other applicable rebates or credits not deducted by the financing institution, over (2) the contract balance, allowable expenses, and amounts paid to discharge any security interest provided for by law.

O. "Pay" or "paid," in reference to payment of a surplus, means a reasonable attempt to pay in accordance with the standards set forth in the Initial Compliance Report.

II.

It is further ordered, That Ford shall provide to all dealers within 60 days of the effective date of this order, and to each new dealer within 30 days of entering into a sales and service agreement, a system for determining the existence of surpluses and for accounting for surpluses and for any deficiencies sought.

A. This system (hereinafter the "accounting system") shall be made a part of the Ford Manual of Dealer Accounting Procedure referred to in the various dealer sales and service agreements between Ford and its dealers. Such agreements provide that this Manual is to be followed in dealership operations. Ford shall not change the sales and service agreements so as to affect the status of the accounting system portion of the Manual without 60 days notice to the Commission and shall not subsequently so change the sales and service agreements so as to affect the status of the Manual if the Commission, within that time period, advises Ford that it objects to the change. The accounting system shall also be incorporated into any subsequent set or compendium of comparable instructions.

B. The accounting system shall include a standardized form ("Ford accounting form") for dealers' use in determining the existence and amount of surpluses and of any deficiencies sought, and in recording payment of each surplus in accordance with the provisions of Paragraph II.C below.

C. The accounting system shall provide that:

1. Each surplus is to be determined according to Paragraphs I.J through I.N of this order and paid to the repurchase financing customer within 45 days of disposition;

2. Expenses other than allowable expenses are not to be deducted in calculating surpluses and deficiencies sought;

3. Dispositions are to be commercially reasonable, which in practice means that the dealer should make the same efforts to obtain the best available price for a repossessed vehicle as would be made for a comparable used vehicle except that a dealer is not required to offer a warranty without extra charge even though such warranties are provided on other used vehicles;

4. If any rebate owing to the repurchase financing customer's account has not been received at the time the Ford accounting form is completed, such rebate is to be applied for promptly;

5. If any rebate is received after completion of the Ford accounting form, any surplus or deficiency is to be redetermined and any remaining surplus paid within 45 days of disposition or within 10 days of receiving the rebate, whichever is later;

6. The Ford accounting form is to be prepared by the dealer for each disposition of a repossessed vehicle and:

a. is to set forth the calculation of each surplus, and of each deficiency upon which collection is attempted;

b. is to be certified by a person authorized to sign retail installment contracts on behalf of the dealership;

c. a copy of the form is to be sent with the surplus payment to each repurchase financing customer to whom a surplus is paid and to each repurchase financing customer from whom a deficiency is sought; and

d. is to be retained by the dealer, together with all relevant underlying documentation, for at least two years from the date of disposition;

7. Dealers are not to obtain waivers of surplus or redemption rights from repurchase financing customers.

D. The accounting system shall state that failure to adhere to the standards of Subparagraphs II.C.1 through II.C.7 or to account properly to customers for surpluses will expose the dealer to legal action by the Federal Trade Commission and/or consumers.

E. Ford shall give the Federal Trade Commission 30 days advance notice of any change in its manner and form of carrying out the requirements of Part II of this order.

F. The accounting system shall not apply to sales of repossessed vehicles subsequent to judicial sales in Louisiana.

G. The Federal Trade Commission has proposed a trade regulation rule that defines duties involved in disposing of a repossessed vehicle differently from the method described in Subparagraph II.C.3 above. Said subparagraph is not to be considered a ratification or acceptance by the Commission of that method of disposition.

III.

A. *It is further ordered,* That the Ford respondents:

1. shall, within 90 days of the effective date of this order, develop and provide to every repurchase dealer detailed educational materials and training to carry out the purposes of Part II of this order and of Part VI (insofar as it relates to reinstatement and redemption rights), as further described in the Initial Compliance Report.

2. shall, commencing no later than 180 days after the effective date of this order, include detailed information on all pertinent aspects of Part II of this order and Part VI (insofar as it relates to reinstatement and redemption rights) in all appropriate seminars, correspondence courses and other training materials offered to dealers.

3. shall provide no instructions to dealers inconsistent with this order.

B. *It is further ordered,* That Ford:

1. shall, within 60 days of the effective date of this order, send to each repurchase dealer a letter which contains information to the following effect, with nothing to the contrary or in mitigation thereof:

a. state law requires that any surplus generated on the disposition of a repossessed vehicle must be returned to the defaulting customer;

b. the duty to pay surpluses has existed for many years and the company urges dealers to pay all surpluses on repossessed vehicles disposed of prior to the date of the letter, as well as those arising later;

c. except in California and Louisiana, state law provides that if a dealer does not pay a surplus owed, the defaulting customer has the right to recover a penalty equal to "an amount not less than the credit service charge plus 10 percent of the principal amount of the debt or the time price differential plus 10 percent of the cash price;"

d. if a customer to whom a surplus is owed has been reported by the dealer or its agent to a credit reporting agency as owing a deficiency, the dealer should promptly advise such agency of the correct facts; and

e. the Federal Trade Commission has issued complaints against three automobile dealers charging that their failure to pay past surpluses violated federal law.

2. shall include in the above mailing a copy of this order, together with the Commission's published Analysis of Consent Order.

3. shall, within 90 days of the effective date of this order, develop and provide to all Ford Dealer Development branch personnel (other than clerical employees) educational materials and training to carry out the purposes of Parts II and V of this order, as further described in the Initial Compliance Report.

4. shall provide to authorized representatives of the Federal Trade Commission upon 30 days written notice a set of mailing labels addressed to the president of each dealership, together with a list containing the same information and a certification that the labels and list are complete.

C. *It is further ordered,* That Ford Credit:

1. shall, within 60 days of the effective date of this order, send to each dealer to which Ford Credit has returned a vehicle, pursuant to a repurchase agreement, that was repossessed since May 1, 1974:

a. a letter containing the same information required by Subparagraph III.B.1 above; and

b. a list containing the following data for each Ford Credit repossession returned to the dealer between May 1, 1974 and the effective date of this order: name, address and account number of the financing customer, net payoff and date of repossession of the vehicle.

2. shall, within 90 days of the effective date of this order, develop and provide to all Ford Credit branch personnel involved in repurchase financing transactions (other than clerical employees) educational materials and training to carry out the purposes of Parts II and VI of this order, as further described in the Initial Compliance Report.

IV.

It is further ordered, That:

A. To determine whether dealers are correctly calculating and paying surpluses, Ford shall conduct an audit ("initial sample audit") of repurchase dealers. This audit shall:

1. consist of 100 repurchase dealers randomly selected pursuant to a sampling method as set forth in the Initial Compliance Report accepted by the Federal Trade Commission;

2. begin within sixteen months after the effective date of this order and be completed and reported to the Federal Trade Commission in accordance with Subparagraph IV.I.2 below within the next eleven months, exclusive of the month of December, as set forth in the Initial Compliance Report.

B. An audit conducted pursuant to Paragraph IV.A or IV.C shall be deemed to demonstrate dealer compliance if less than 1.5 percent of the dispositions audited are noncomplying transactions. A "noncomplying transaction," as further described in the Initial Compliance Report, means a disposition that results in a surplus not correctly calculated and paid in full to the financing customer.

C. In the event the initial sample audit does not demonstrate dealer compliance Ford shall conduct further audits ("follow-up sample audits"), each to consist of 85 dealers randomly selected pursuant to the procedure and schedule described in the Initial Compliance Report, until an audit demonstrating dealer compliance has been attained or a total of four follow-up sample audits have been conducted, whichever occurs first.

D. Within thirty days after a determination by Ford or advice by the Commission's representatives that the initial sample audit or a follow-up sample audit does not demonstrate dealer compliance, Ford shall supplement the accounting system to provide that each dealer submit to Ford:

1. no later than six months after the above advice or determination, the completed Ford accounting forms described in Paragraph II.B of this order for all repurchase financing repossessions disposed of by the dealer that were returned to the dealer during the audit period covered by the prior sample audit; and

2. with each of the above submissions, a signed statement that the Ford accounting forms submitted include all repurchase financing repossessions disposed of by the dealer that were returned to the dealer during the audit period or, alternatively, that there were no such repossessions.

No submission shall be necessary after the last follow-up sample audit.

E. Ford shall review all Ford accounting forms submitted to it pursuant to Paragraph IV.D within 90 days of their receipt. This review shall be conducted by trained clerical personnel in accordance with the Initial Compliance Report, but Ford shall not be required to undertake a detailed analysis of these Ford accounting forms and shall not be deemed to have violated this paragraph if, despite good faith efforts, there are errors or omissions in that review.

F. Three years after completion of the last audit required pursuant to Paragraph IV.A or IV.C, Ford shall conduct a "final sample audit" of 85 randomly selected dealers pursuant to the procedure and schedule described in the Initial Compliance Report.

G. In addition to the audits provided for above, Ford shall conduct a supplemental audit of each dealership:

1. found by Ford, in the immediately preceding initial sample audit or follow-up sample audit of the dealership, to have had noncomplying transactions as set forth in the Initial Compliance Report;

2. which failed to submit either the Ford accounting forms required by Paragraph IV.D or a signed statement that no repurchase financing repossessions were returned to the dealership during the relevant period;

3. which failed to indicate payment of a surplus identified on any Ford accounting form submitted pursuant to Paragraph IV.D;

4. which failed more than occasionally, as further described in the Initial Compliance Report, to sign the certification on Ford accounting forms submitted pursuant to Paragraph IV.D; or

5. found, based on review of the Ford accounting forms submitted pursuant to Paragraph IV.D, to have deducted expenses other than allowable expenses.

Each supplemental audit required by this paragraph shall be completed within six months of detection of the event which triggers it and shall be conducted pursuant to the procedure set forth in the Initial Compliance Report.

H. Within sixty days after completion of each audit of a dealership provided for in Paragraphs IV.A, C, F and G above, Ford shall:

1. submit to the Federal Trade Commission a summary report of the audit for that dealership, containing: (a) the name and address of the dealership; (b) the number of dispositions examined; (c) the number and dollar value of surpluses properly calculated and paid; (d) the number and dollar value of surpluses as to which attempts to pay were unsuccessful; (e) the number of repossessed vehicles sold at wholesale; (f) the number of noncomplying transactions and, for each such transaction, the amount owed, copies of the audit worksheets, the Ford accounting form and business records of the dealership and/or financing institution sufficient to establish such noncompliance; and (g) a certification by the auditor attesting to his or her findings concerning each noncomplying transaction, including the reason for noncompliance and any explanation provided by the dealership; and

2. for each dealership found to have noncomplying transactions as set forth in the Initial Compliance Report, commence further dealership training to correct such noncompliance.

I. The audits provided for in Paragraphs IV.A, C, and F of this order shall conform to Subparagraphs 1–7 below. The audits conducted pursuant to Paragraph IV.G shall conform to Subparagraphs 3–7 below. The audits and report submissions provided for in Paragraphs IV. C, D, E and G shall also conform to Subparagraph 8 below.

1. The Federal Trade Commission shall be given reasonable advance notice of the time of random selection and shall have the opportunity to have its representatives observe and review the random selection process.

2. Ford shall provide to the Commission a summary report of each entire sample audit, within 60 days after completion of such audit, specifying (a) the name and address of each dealership included, (b) the total number of dispositions examined, (c) the total number and dollar value of noncomplying transactions, (d) the number and dollar value of surpluses properly calculated and paid, (e) the number and dollar value of surpluses as to which attempts to pay were unsuccessful, and (f) the number of repossessed vehicles sold at wholesale.

3. For each dealer audited, each repurchase financing repossession returned to the dealer during the audit period shall be examined to determine whether it is a noncomplying transaction.

4. The audit shall be conducted by the General Auditor's Office of Ford Motor Company (or by other qualified auditors designated by Ford), in accordance with the procedure described in the Initial Compliance Report.

5. The Ford respondents shall direct their personnel (including retained consultants or experts) that they are not to inform dealers or other third parties of the audit procedure, the sample period, the method of drawing the sample, or the identity of dealers selected for audit except to the extent described in this order, and the Ford respondents shall take all reasonable measures to ensure that their personnel adhere to this direction.

6. No dealer selected for audit shall be given more than ten business days advance notice of the scheduled audit.

7. Upon request by the Commission's representatives, Ford shall, within 30 days, submit copies of the auditors' worksheets and summary comments on any dealership audited.

8. In particular circumstances of dealer noncompliance, the

schedule and scope of audits and report submissions shall be modified as described in the Initial Compliance Report.

V.

It is further ordered, That Ford:

A. Shall require each Ford employee who is a director of an equity dealership to vote for resolutions so that each such dealership:

1. within 60 days of the effective date of this order or within 60 days of initiating operation as a dealership, whichever is later, adopts and maintains the accounting system described in Part II of this order;

2. pays all surpluses (*provided, however,* that a dealership's failure to pay a surplus which has not come to the attention of any Ford employee whose primary responsibilities concern equity dealerships shall not be deemed a violation of this subparagraph); and

3. has an annual examination of its documents by a certified public accounting firm, for each year up to and including the year that the final sample audit is completed, to determine whether the dealership is following the accounting system; such examination shall (a) include an inspection of underlying documents supporting entries on the Ford accounting form (described in Paragraph II.B of this order) for all repossessed vehicles returned to the dealership during the year covered by the examination and (b) be followed by a report to the dealership board of directors regarding any noncomplying transactions.

B. Shall require that, at every accounting review of an equity dealership, but in any event at least once every calendar year commencing after the effective date of this order, Ford's employees shall randomly select and examine underlying documents supporting entries on the Ford accounting form for at least one-fourth of the repossessed vehicles returned to the dealership since the previous such review or since January 1, 1978, whichever is later. If the examination reveals that the dealership has any noncomplying transactions, then:

1. Ford's employees shall examine underlying documents for the remaining three-fourths of the repossessions and report all noncomplying transactions to the dealership's board of directors; and

2. Ford employees who are members of such board of directors shall institute appropriate measures to correct the noncompliance.

C. Shall ascertain for each liquidating dealership whether any unpaid surpluses have arisen since the last audit by an independent certified public accounting firm, and pay each such surplus.

D. Shall, within 60 days of the effective date of the order, with respect to repossessed vehicles returned between May 1, 1974 and December 31, 1977 to dealerships which are equity dealerships as of the effective date of this order, and with respect to repossessed vehicles returned between May 1, 1974 and December 31, 1977 to liquidating dealerships, establish to the reasonable satisfaction of the Commission, as described in the Initial Compliance Report, that:

1. all surpluses have been paid; and
2. in each instance where a customer entitled to receive a surplus pursuant to Subparagraph V.D.1 above had been previously reported by the dealership or its agent to a credit reporting agency as owing a deficiency, such agency has been subsequently advised of the correct facts.

VI.

It is further ordered, That Ford Credit:

A. Shall incorporate provisions to the following effect into the "Retail Plan" section of its "Automotive Finance Plans for Ford Motor Company Dealers," within 60 days of the effective date of this order, and into any subsequent edition of that document or any comparable successor document:

1. dealers are to permit redemption by the customer whose vehicle has been repossessed, at any time until there is a binding agreement for disposition;
2. dealers are to permit redemption in accordance with the post-repossession notice sent by Ford Credit to the customer;
3. dealers are to determine whether a surplus exists on a repurchase financing repossession according to the accounting system described in Part II of this order;
4. in determining surpluses and deficiences, dealers are not to deduct expenses other than allowable expenses;
5. dealers are to account for and pay each surplus within 45 days of disposition.

B. Shall, as soon as practicable, but no later than twelve months after the effective date of this order, develop and distribute to all dealers who use Ford Credit's form of retail installment contract, revised Ford Credit retail installment contract forms that include a clear, concise statement in lay language that, in the event of repossession:

1. no expenses other than reasonable expenses incurred as a direct result of repossessing (including, where permitted, attorney's fees and court costs), holding, preparing for sale and selling the vehicle may be deducted from the proceeds in determining a surplus or deficiency; and

2. any surplus realized on the resale or other disposition of the vehicle is to be paid to the customer.

C. Shall direct its branch offices that, commencing two weeks after the distribution to a dealership of the revised Ford Credit retail installment contract forms described in Paragraph VI.B, they are not to purchase from that dealership Ford Credit forms of retail installment contracts that are not on the revised forms and shall, for a period of two years thereafter, periodically examine its branch office files, in accordance with its usual monitoring procedures, to determine whether prior retail installment contract forms are being used, and, if so, shall institute appropriate corrective action.

D. Shall, commencing 75 days after the effective date of this order, include the following information in clear lay language in at least one notice sent prior to repossession to every Ford Credit repurchase financing customer to whom a notice of intent to repossess is sent:

1. the total amount past due at the time the notice is mailed;

2. in transactions where the customer is entitled to reinstatement of the contract, the customer will have an absolute right to such reinstatement and to regain possession of the vehicle by paying all past due installments and by paying such other amounts and fulfilling such other conditions as provided by law;

3. that the customer will have an absolute right to redeem the vehicle at any time prior to a binding agreement for its disposition, and that this right can be exercised by paying the contract balance plus all expenses incurred as a direct result of repossessing, holding and preparing the vehicle for sale;

4. the date or interval of time prior to which the vehicle will not be sold;

5. that if the vehicle is not redeemed or the contract reinstated, the customer will be entitled to a refund of any surplus within 45 days of disposition;

6. that failure to account for and refund a surplus will give the customer a right to sue for the amount of the surplus and, except in California and Louisiana, for statutory penalties as provided by state law.

E. Shall, within 60 days after the effective date of this order, establish and follow a procedure for uniformly sending a written notice ("post-repossession notice") to Ford Credit financing customers as soon as practicable after repossession. Ford Credit shall periodically examine its branches' files, in accordance with its usual monitoring procedures, to determine whether the post-repossession notices have been and are being sent, and shall institute appropriate actions to assure that this procedure is adhered to. In the event of any charge of failure to follow the procedure for uniformly sending post-repossession notices, Ford Credit shall not be deemed in violation unless it is shown that Ford Credit has failed to send such notices at least ten days prior to the earliest resale date stated pursuant to Subparagraph VI.E.4 below on more than five percent of the repossessions of each of three Ford Credit branch offices in any twelve-month period. The post-repossession notice shall specify in clear, lay language:

1. the name, address and telephone number of the dealership to which the vehicle has been or will be returned for disposition, if applicable, and the address and telephone number of the Ford Credit branch office to be contacted;

2. the date or interval of time within which the customer may reinstate the contract in states where the creditor is required to permit reinstatement of the contract;

3. the net amount necessary to redeem the vehicle, and, in transactions where the customer is entitled to reinstatement, the amount necessary to reinstate the contract, at the time the notice is sent;

4. the date or interval of time prior to which the vehicle will not be sold;

5. that the vehicle can be redeemed at any time prior to a binding agreement for its disposition;

6. that additional expenses incurred as a direct result of holding and preparing the vehicle for sale may increase the amount necessary to redeem the vehicle if redemption is delayed;

7. that Ford Credit should be contacted to reinstate the contract in states where the customer is entitled to reinstatement;

8. that Ford Credit should be contacted for further information about redemption including the procedure for redeeming the vehicle;

9. that, where the vehicle has been returned to the dealer and is not redeemed or the contract is not reinstated, any surplus must be paid to the customer within 45 days after disposition (the notice may also state that a contract between the dealer and Ford Credit provides that the dealer is to pay any surplus);

10. that failure to account for and refund a surplus will give the customer a right to sue for the amount of the surplus and, except in California and Louisiana, for statutory penalties as provided by state law;

11. that the customer may be liable for a deficiency or that state law prohibits Ford Credit and the dealer from collecting any deficiency (the notice is to include the applicable language only);

12. that the customer has the right to direct the dealer to apply for a rebate of any unearned premiums payable by any insurance carrier or agent from whom the dealer has, on behalf of the customer, obtained a credit life, accident and health or collision insurance policy.

F. Shall obtain no waivers of redemption or surplus rights from financing customers.

G. Shall, commencing three months and to be completed no later than twelve months after the effective date of this order, revise all pertinent Ford Credit forms, form letters, notices and internal written procedures to be consistent with the provisions of this order.

VII.

It is further ordered, That:

A. In the event the Federal Trade Commission issues a final trade regulation rule establishing standards less restrictive on automobile manufacturers, financing companies or vehicle dealerships than a corresponding provision or provisions of this order relative to (1) the disposition of repossessed vehicles, (2) the determination, calculation or communication of the existence of or the amount of surpluses, or the time or manner of paying or accounting for surpluses, or (3) the determination or communication of reinstatement or redemption rights (including their duration and/or the amount necessary to reinstate or redeem), then such less restrictive standards shall, on the effective date of the rule, supersede and replace the corresponding provision(s) of this order. The enumeration of subject matter contained in clauses (1), (2) and (3) of this paragraph is exclusive. *Provided, however,* that the Ford respondents shall advise the Commission of their intention to rely upon any provision of a trade regulation rule as having superseded any provision of this order 30 days in advance of reliance thereon. *Provided further,* that this paragraph shall not be construed as exempting the Ford respondents from any trade regulation rule, or as limiting in any way their legal right or standing to challenge or otherwise contest any trade regulation rule.

B. In the event any of the proceedings presently bearing Dkts. 9072, 9073, or 9074 results in a final adjudicated or consent order prescribing standards less restrictive than a corresponding provision or provisions of this order relative to (1) the disposition of repossessed vehicles, (2) the determination, calculation or communication of the existence of or the amount of surpluses, or the time or manner of paying or accounting for surpluses, or (3) the determination or communication of reinstatement or redemption rights (including their duration and/or the amount necessary to reinstate or redeem), then the Commission shall, within 120 days of a Ford respondent's petition pursuant to Section 3.72 of the Commission's Rules of Practice, reopen this proceeding and order modifications of this order or other relief as necessary and appropriate to conform this order to such less restrictive standards prescribed in the other order(s). The enumeration of subject matter contained in clauses (1), (2) and (3) of this paragraph is exclusive.

C. In the event a Ford respondent is of the opinion that changed conditions of law require that this order be altered or modified, the Ford respondent may, pursuant to Section 3.72(b)(2) of the Commission's Rules of Practice, file a petition requesting a reopening of this proceeding for that purpose.

VIII.

It is further ordered, That:

A. The Ford respondents shall maintain complete business records relative to the manner and form of their continuing compliance with this order, including but not limited to copies of notices sent to financing customers pursuant to Paragraphs VI.D and E above, and records prepared pursuant to Paragraphs V.A-C for each equity and liquidating dealership. The Ford respondents shall retain all such records for at least three years and shall, upon reasonable notice, make them available for inspection and photocopying by authorized representatives of the Federal Trade Commission.

B. Each of the Ford respondents shall, within 120 days after the effective date of this order, file with the Commission a written report setting forth in detail the manner and form in which it has complied with this order and has implemented the Initial Compliance Report submitted with the Agreement Containing Consent Order.

C. Ford shall forthwith distribute a copy of this order to its Ford, Lincoln-Mercury and Parts and Services divisions, and to the Dealer Development activity, and Ford Credit shall forthwith distribute a copy of this order to each of its Regions.

D. Each of the Ford respondents shall notify the Commission at least thirty days prior to any proposed corporate change such as dissolution, assignment or sale resulting in the emergence of a successor corporation or corporations, the creation or dissolution of subsidiaries, the discontinuance of Ford's present program for investing in equity dealerships, or any other change which may affect compliance obligations arising out of this order.

IN THE MATTER OF

ROYAL FURNITURE CO., INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND TRUTH IN LENDING ACTS

Docket 9090. Complaint, Oct. 26, 1976 — Decision, March 29, 1979

This consent order, among other things, requires a Bronx, N.Y. furniture and appliance retailer to cease failing to advise consumers that co-signers may be required in credit transactions; signed documents are not final until they have been approved; and that customers may, upon denial of credit, cancel their purchases and receive refunds of downpayments. The Company is required to honor valid cancellations; make proper refunds; and furnish consumers with credit disclosures required by Federal Reserve System regulations and booklets outlining their legal and contractual rights. Additionally, the firm is prohibited from engaging in harassing debt collection practices, including false threats of repossession and garnishment; and improper third-party contact. The order also requires the firm to establish procedures for handling complaints regarding defective, damaged or nonconforming merchandise; and maintain specified records.

Appearances

For the Commission: *Henry R. Whitlock* and *Sandra L. Bird.*

For the respondents: *Howard Mann, Weiss, Rosenthal, Heller, Schwartzman & Lazar,* New York City.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, and of the Truth in Lending Act and the implementing regulation promulgated thereunder, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission having reason to believe that Royal Furniture Co., Inc., a corporation, and Milton Landes, individually and as an officer of said corporation, hereinafter referred to as respondents, have violated the provisions of said Acts, and of the regulation promulgated under the Truth in Lending Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. For the purpose of this complaint and the proposed order attached hereto, the following definitions of terms shall apply:

1. "Consumer" refers to a natural person who seeks or acquires goods, services or money for personal, family or houshold use.

2. "Co-signer" refers to a natural person who, by agreement, and without compensation, renders himself liable for the credit purchases of a consumer.

3. "Retail Installment Credit Agreement" refers to a written agreement pursuant to which respondents extend credit to consumers for the present and future purchase of respondents' merchandise.

4. "Debt collection" refers to any activity other than the use of judicial process which is intended to bring about or does bring about repayment of all or part of a consumer debt, except:

(1) Inquiry to locate a consumer whose whereabouts are genuinely unknown to the creditor; and/or

(2) Inquiry to determine the nature and extent of a consumer's wages or property;

Provided that, in these two instances, no specific mention is made of the alleged indebtedness.

PAR. 2. Respondent Royal Furniture Co., Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York with its principal office and place of business located at 2936 Third Ave., Bronx, New York.

Respondent Milton Landes is an officer of the corporate respondent. He formulates, directs and controls the acts and practices of the corporate respondent, including the acts and practices hereinafter set forth. His business address is the same as that of the corporate respondent.

PAR. 3. Respondents are now, and for some time last past have been, engaged in the purchasing, advertising, offering for sale, sale and distribution of furniture, appliances and related products to the public at retail.

COUNT I

Alleging violation of Section 5 of the Federal Trade Commission Act, as amended, the allegations of Paragraphs Two and Three hereof are incorporated by reference herein as if fully set forth verbatim.

PAR. 4. Respondents maintain and have maintained a substantial course of business including the acts and practices, as hereinafter set forth, which are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 5. In the course and conduct of their aforesaid business, and for the purpose of inducing the purchase of their merchandise, respondents, through advertising brochures and oral statements of respondents' salesmen, employees or representatives (hereinafter referred to as "representatives") have made, and continue to regularly make, numerous and various statements and representations concerning the terms and methods of payment, and the availability of credit for the purchase of respondents' merchandise.

Typical and illustrative of the foregoing, but not all inclusive thereof, are the following statements often used in conjunction with one another by their being interspersed throughout respondents' advertising brochures:

- Use Royal's Easy Credit
- Budget Terms
- Budget Accounts Invited at Royal
- Royal Welcomes People on Welfare, Social Security and Pensions, Newlyweds, Students and Teenage Accounts, Civil Service Employees and Union Members
- Terms especially made to fit your budget
- Low downpayment, convenient credit terms
- Arrange your own downpayment
- Use your credit
- House Full of Luxury – Instant Credit Too

PAR. 6. By and through the use of the above-quoted statements and representations and others of similar import and meaning not specifically set out herein, respondents have represented and continue to represent, directly or by implication, that:

1. Respondents offer liberal policies with regard to the extension of credit, downpayments required, terms and conditions of repayment of the indebtedness and/or collection practices.

2. Respondents offer personalized credit and allow their customers to arrange downpayments, payment schedules and credit terms to suit the customer's own financial needs and budget limitations.

3. Customers on low and fixed incomes can establish their own credit accounts.

4. Customers will be given immediate credit from respondents without difficulty.

PAR. 7. In truth and in fact:

1. Respondents do not offer liberal credit terms and customers who fall behind in their payments are subjected to late charges and strict collection practices including law suits.

2. Respondents do not offer personalized credit terms and do not

allow their customers to determine the amount of the downpayment, payment schedule, or credit terms.

3. In many instances customers with low and fixed incomes are not extended credit solely on their own account and must secure one or more co-signers.

4. In many instances, credit is not extended immediately or is withdrawn or otherwise subjected to conditions subsequent to respondents' acceptance of the credit transaction or execution of the contract.

PAR. 8. Therefore, the aforesaid statements, representations, acts and practices regarding the terms, conditions and availability of credit offered by respondents were and are, false, misleading and deceptive, in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT II

Alleging violation by respondents of Section 5 of the Federal Trade Commission Act, as amended, the allegations of Paragraphs Two through Eight hereof are incorporated by reference herein as if fully set forth verbatim.

PAR. 9. In the further course and conduct of their business as aforesaid, respondents use a form printed on two sides, the front serving as respondents' sales slip and the back containing respondents' Retail Installment Credit Agreement.

The sales slip on the front of said form sets forth a description and price of the consumers' present purchases, downpayment, if any, the balance owed and the amount and time schedule for the consumer's minimum periodic payments.

The Retail Installment Credit Agreement on the back of said form sets forth the terms under which respondents are extending credit to the consumer for his present and future purchases. Such terms include, but are not limited to, the amount and method of assessing finance charges, acceleration of balance due upon default, and liability for attorney's fees. The Retail Installment Credit Agreement incorporates by reference the terms set forth on the sales slip.

PAR. 10. By virtue of respondents' false, misleading and deceptive representations, acts and practices as set forth in Paragraphs Five and Six, consumers have been induced to order merchandise on credit and in regard thereto have paid substantial sums of money to respondents as deposits or downpayments and have entered into Retail Installment Credit Agreements as described herein with respondents.

In many instances, at the time the credit agreements are entered into, respondents represent, directly or by implication, that the sales slips and the credit terms contained in the Retail Installment Credit Agreements have been accepted by or on behalf of respondents, and that the sales have been consummated in mutually binding agreements.

PAR. 11. In many instances, after having received moneys from consumers as deposits or downpayments for merchandise, respondents have failed or refused to honor the terms of the agreement by conditioning delivery of merchandise upon consumers paying larger downpayments or deposits, obtaining co-signers or agreeing to purchase less expensive merchandise than originally ordered.

Therefore respondents' aforesaid misrepresentation that the sales slips and the Retail Installment Credit Agreements between themselves and consumers mutually bind the store and the customer was and is a false, misleading and deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended, and respondents' failure or refusal to honor their agreements with consumers to deliver the merchandise originally ordered by consumers on the credit terms originally agreed upon was and is an unfair act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

PAR. 12. In the further course and conduct of their business, as aforesaid, in many instances respondents, directly or indirectly, have told consumers who did not agree to the foregoing changes in the terms of either their sales slips or Retail Installment Credit Agreements that respondents would not cancel said consumers' contractual obligations, and/or would not refund any moneys already paid to respondents.

Therefore, the aforesaid act or practice was and is an unfair practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

PAR. 13. As a result of the foregoing respondents have (a) induced and are inducing members of the public through unfair and deceptive acts and practices to pay to respondents substantial sums of money towards the purchase of respondents' merchandise, and (b) have continued to retain substantial sums of said monies and/or have continued to refuse to cancel contractual obligations.

PAR. 14. The use by respondents of the aforesaid acts and practices, including their continued refusal to honor their agreements with consumers on the credit terms originally agreed upon and their continued retention of said sums and their continued refusal to cancel contractual obligations of their customers, was and is unfair and injurious to the public in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT III

Alleging violation by respondents of Section 5 of the Federal Trade Commission Act, as amended, the allegations of Paragraphs Two through Fourteen hereof are incorporated by reference herein as if fully set forth verbatim.

PAR. 15. In the further course and conduct of their business as aforesaid, respondents, in many instances, have required consumers, who want to purchase merchandise on credit, to obtain one or more persons to act as co-signers of the Retail Installment Credit Agreement between respondents and said consumers. The persons acting as co-signers are designated as co-buyers on the Retail Installment Credit Agreements, but in most instances respondents treat said persons as co-signers.

PAR. 16. In most instances where respondents have required co-signers as aforesaid, respondents have not, prior to said co-signers becoming obligated, either orally or in a writing readily understandable to a person without legal experience or background, disclosed to the co-signers their legal obligations and rights as co-signers and which, if any, of the terms and conditions of the Retail Installment Credit Agreements apply to co-signers.

PAR. 17. Respondents have further failed to disclose to potential co-signers that, in many instances, respondents have:

1. Sued co-signers for the unpaid balance owed by consumers plus accrued finance charges and attorney's fees.
2. Applied the technical terms of the Retail Installment Credit Agreements, such as those terms specifically listed in Paragraph Nine above, to the co-signers.
3. Sued co-signers without giving them any notice of consumers' defaults or an opportunity to pay prior to suit.
4. Sued co-signers in the same action as consumers and enforced the judgment obtained against co-signers prior to or simultaneously with enforcement against consumers.

Thus respondents have failed to disclose material facts which if known to certain co-signers would likely affect their decision to become co-signers of respondents' Retail Installment Credit Agreements.

PAR. 18. Therefore respondents' failure to disclose material facts as to the obligations of the aforesaid co-signers and possible

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consequences of their agreement, prior to the completion of the credit sale and in a meaningful manner and in clear, plain language, was and is unfair, misleading and deceptive and constituted and now constitutes an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT IV

Alleging violation by respondents of Section 5 of the Federal Trade Commission Act, as amended, the allegations of Paragraphs Two through Eighteen hereof are incorporated by reference herein as if fully set forth verbatim.

PAR. 19. In the course and conduct of their business as aforesaid, in instances where respondents have required consumers to provide one or more co-signers on respondents' Retail Installment Credit Agreements, respondents have often further required said co-signers to sign a Continuing Guarantee and Waiver containing, inter alia, the following provisions:

1. The co-signer guarantees payment for any future indebtedness contracted by the consumer for two years from the date of the guarantee, up to a specified maximum amount.
2. The co-signer waives the sending of notice to himself of a default on the part of the consumer.
3. The contract of guarantee is irrevocable as to future credit purchases for a two year period.
4. The co-signer agrees to pay all present or future indebtedness without first requiring the respondents to seek payment from the consumer.

PAR. 20. By and through the use of the aforementioned Continuing Guarantee and Waiver respondents:

1. Extend the co-signer's obligation beyond the amount specified in the original sales contract to include all future credit purchases of the consumer for a two year period, and up to a specified maximum, without the co-signer's specific knowledge of or control over the amount, frequency or terms of said purchases, and without said co-signer having an opportunity to re-evaluate the consumer's ability to pay for future purchases.
2. Deny the co-signer any opportunity to attempt to rectify a default prior to his being sued.
3. Prevent the co-signer from cancelling his future liability upon a change in either the consumer's or the co-signer's financial situation.

4. Place the co-signer in a position where he may be held primarily and/or solely liable for the debts of another.

PAR. 21. The aforementioned obligations and liabilities are not bargained for provisions and are not generally understood by persons without legal experience and background.

PAR. 22. Therefore, the use by respondents of the Continuing Guarantee and Waiver in which co-signers may be held primarily and/or solely liable for respondents' customers' debts, under the terms described herein, was and is an unfair act and practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT V

Alleging violation by respondents of Section 5 of the Federal Trade Commission Act, as amended, the allegations of Paragraphs Two through Twenty-Two hereof are incorporated by reference herein as if fully set forth verbatim.

PAR. 23. In the further course and conduct of their business as aforesaid, in most of the instances where respondents have required that co-signers sign the aforementioned Continuing Guarantee and Waiver, respondents have not, prior to the co-signers signing, either orally or in a writing readily understandable to a person without legal experience or background, disclosed to the co-signer his legal obligations and rights under the technical terms of the Continuing Guarantee and Waiver as set forth more fully in Paragraphs Nineteen and Twenty.

PAR. 24. The circumstances surrounding the credit transaction as set forth more fully in Paragraphs Fourteen, Fifteen and Sixteen herein and the failure of respondents to meaningfully disclose to co-signers their legal obligations and rights under the Continuing Guarantee and Waiver, has the tendency and capacity to mislead prospective co-signers into the mistaken belief that: co-signers are liable to pay only for consumers' purchases listed on the form serving as respondents' sales slip, as described in Paragraph Fourteen herein.

Thus, respondents have failed to disclose material facts, which, if known to certain co-signers, would likely affect their consideration of whether or not to act as co-signers of credit sales with respondents.

PAR. 25. Therefore respondents' failure to disclose the aforementioned material facts in a meaningful manner and in plain language, prior to the completion of credit sales, was and is unfair, misleading and deceptive and constituted and now constitutes an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT VI

Alleging violation by respondents of Section 5 of the Federal Trade Commission Act, as amended, the allegations of Paragraphs Two through Twenty-Five are incorporated by reference herein as if fully set forth verbatim.

PAR. 26. In the further course and conduct of their business as aforesaid, in those instances where respondents have required co-signers to sign Retail Installment Credit Agreements and/or Continuing Guarantees and Waivers, respondents have often failed to furnish the aforesaid co-signers with copies of all the agreements they have signed in the credit transaction.

PAR. 27. Therefore the aforesaid act or practice was and is unfair in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT VII

Alleging violation of Section 5 of the Federal Trade Commission Act, as amended, Paragraphs Two through Twenty-Seven hereof are incorporated by reference as if fully set forth herein verbatim.

PAR. 28. In the course and conduct of their business as aforesaid, respondents in numerous instances have commenced legal proceedings to collect monies owed respondents under the terms of the Retail Installment Credit Agreements and/or Continuing Guarantee and Waivers.

PAR. 29. Subsequent to the service and filing of the summons in the aforementioned legal proceedings, respondents in many instances, directly or by implication, have advised persons who have been sued and who contact respondents concerning the action, to continue making payments and to ignore summonses or other legal notices. In connection with the aforesaid, respondents have accepted and/or agreed to accept payments from consumers and co-signers, and have failed to file with the court a notice of discontinuance, settlement or any other papers which would indicate that an agreement has been reached between the parties to the action. As a result of, and in reliance on, such deceptive or misleading representations, the aforementioned persons default in appearing in said action, or fail to take other necessary legal action.

PAR. 30. The legal consequences as well as the potential effect on an individual's credit rating of failing to appear in legal proceedings, of failing to file documents showing that a case has been settled or discontinued and of failing to take other affirmative legal actions, are not generally known or understandable to persons without legal experience or background.

PAR. 31. As a result of the foregoing respondents have (i) induced and are inducing members of the public through unfair and deceptive acts and practices to pay to respondents substantial sums of money towards the purchase of respondents' merchandise, and (ii) have continued to accept and retain payments from persons whom they advised, directly or by implication, to ignore court summonses and other legal papers while respondents have proceeded with their legal suits against these persons or have failed to discontinue or formally settle said legal suits.

The use by respondents of the aforesaid acts and practices, was and is an unfair and deceptive act or practice to the injury of the public in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT VIII

Alleging violation of Section 5 of the Federal Trade Commission Act, as amended, the allegations of Paragraphs Two through Four hereof are incorporated by reference herein as if fully set forth verbatim.

PAR. 32. In the course and conduct of their aforesaid business, and for the purpose of inducing the sale of their merchandise, respondents, in their salesrooms and warehouse, have maintained, and are now maintaining, floor models and displays of merchandise being offered for sale, on the basis of which their customers select and order such merchandise.

In this connection, respondents and their sales representatives have made, and are now making, numerous oral statements and representations to customers and prospective customers regarding the quality and durability of merchandise being offered for sale, the terms and conditions under which merchandise will be sold and delivered and the services that will be provided by the respondents.

Moreover, subsequent to making sales and deliveries, respondents and their representatives have made, and are now making, numerous oral statements, representations and promises to their customers regarding the time and the manner in which respondents will perform various adjustments, replacements and repairs.

PAR. 33. By and through the use of the aforementioned floor models and displays, together with the aforesaid oral statements, representations and promises made by respondents, their sales representatives and other employees, respondents have represented, and are now representing, directly or by implication, that:

1. Merchandise delivered will conform in color, material, style, quantity and quality to that ordered.
2. Merchandise sold by respondents will be delivered to the customer free from damage and defects.
3. Merchandise which is delivered to purchasers with damages or defects or which does not conform to the merchandise ordered, will be repaired or replaced within a reasonable time.
4. Merchandise which is delivered to purchasers with damages or defects or which does not conform to the merchandise ordered will be repaired or replaced to the satisfaction of the purchaser.

PAR. 34. In truth and in fact:

1. In many instances, merchandise delivered does not conform in color, material, style and quality to that ordered.
2. In many instances, merchandise sold by respondents is delivered to purchasers with damages and/or defects.
3. In many instances, merchandise which is delivered to purchasers with damages and/or defects and/or does not conform to the merchandise ordered is not repaired or replaced within a reasonable time.
4. In many instances, merchandise which is delivered to purchasers with damages and/or defects and/or does not conform to the merchandise ordered is not repaired or replaced to the satisfaction of the purchasers.

PAR. 35. Therefore, the aforesaid statements, representations, acts and practices regarding respondents' products and services, were and are, false, misleading and deceptive, in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT IX

Alleging violation of Section 5 of the Federal Trade Commission Act, as amended, the allegations of Paragraphs Two through Four and Thirty-Two through Thirty-Five hereof are incorporated by reference herein as if fully set forth verbatim.

PAR. 36. By virtue of respondents' misleading, deceptive and false representations, acts and practices, set forth in Count VIII customers have been induced to pay substantial sums of money to respondents for furniture and other merchandise. Respondents have received said sums and have failed or refused, and continue to fail or refuse, to repair or replace, or make refunds for, damaged, and/or defective and/or non-conforming merchandise, or to honor the implied warranties imposed by law upon such sales.

PAR. 37. Therefore, the use by the respondents of the aforesaid practices was and is an unfair act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT X

Alleging violation of Section 5 of the Federal Trade Commission Act, as amended, the allegations of Paragraphs Two through Thirty-One hereof are incorporated by reference herein as if fully set forth verbatim.

PAR. 38. In the further course and conduct of their business, respondents and their representatives have engaged in a variety of harrassing and threatening debt collection activities including but not limited to the following:

1. Telephone calls to consumers and consumers' neighbors threatening repossession or seizure of merchandise purchased from respondents.
2. Telephone calls to consumers threatening immediate wage garnishment and other extraordinary action prior to institution of legal proceedings.
3. Telephone calls to consumers and their neighbors, friends and employers by persons representing themselves as New York City marshals, sheriffs or attorneys or other state or local officials.
4. Mailing to allegedly delinquent consumers a "Speed-O-Gram" which by its color and appearance, styling, printing and format simulates a telegraphic message.

PAR. 39. In truth and in fact:

1. Respondents have not caused repossession or seizure and under state law, respondents have no legal right to cause repossession or seizure of merchandise purchased in a retail installment credit transaction prior to obtaining a final judgment in a legal proceeding.
2. Respondents have not caused immediate wage garnishment or other extraordinary action and under state law respondents have no legal right to cause wage garnishment or other extraordinary action prior to obtaining a final judgment in a legal proceeding.
3. In many instances telephone calls to consumers, their neighbors, friends and employers, by persons claiming to be New York

City marshals, sheriffs or attorneys or other state or local officials are not made by such persons but are made by respondents and their representatives.

4. The "Speed-O-Gram" is not a telegraphic message; rather it is a form collection letter sent through the regular United States mail which because of its simulation misleads the recipient as to its nature, import, purpose and urgency.

Therefore, the statements and representations set forth in Paragraph Thirty-Eight are false, misleading and deceptive.

PAR. 40. In the further course and conduct of their debt collection activities respondents or their representatives have:

1. Telephoned alleged debtors' neighbors and friends and made specific mention of the alleged indebtedness.

2. Telephoned alleged debtors' places of employment and made specific mention of the alleged indebtedness to persons other than the alleged debtors.

PAR. 41. Respondents' aforementioned conduct has the capacity directly or indirectly to jeopardize consumers' employment, cause embarrassment and damage to reputation and to coerce consumers to make payments of amounts allegedly owed and/or to forego or waive defenses.

Therefore the aforementioned acts and practices are unfair.

PAR. 42. In some instances respondents have engaged in the debt collection activities set forth in Paragraphs Thirty-Eight and Forty and/or have instituted legal proceedings against consumers while there is a dispute between respondents and consumers as to acceptability of merchandise or repairs, and/or correctness of billing. Said conduct has the capacity directly or indirectly to coerce consumers to make payments of amounts allegedly owed and/or to forego or waive defenses.

Therefore respondents' aforesaid acts and practices are unfair.

PAR. 43. Therefore, the representations, acts and practices set forth herein are unfair, false, misleading and deceptive in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT XI

Alleging violation of Section 5 of the Federal Trade Commission Act, as amended the allegations of Paragraphs Two through Forty-Three hereof are incorporated by reference herein as if fully set forth verbatim.

PAR. 44. In the course and conduct of their business as aforesaid, and at all times mentioned herein, respondents have been, and now are, in substantial competition in or affecting commerce with corporations, firms and individuals engaged in the sale of merchandise of the same general kind and nature as merchandise sold by respondents.

PAR. 45. The use by respondents of the aforesaid false, misleading and deceptive statements, representations, acts and practices, directly or by implication, has had, and now has, the capacity and tendency to mislead members of the purchasing public into the erroneous and mistaken belief that said statements and representations were, and are, true and complete, and into the purchase of substantial quantities of respondents' products and services by reason of said erroneous and mistaken belief.

PAR. 46. The acts and practices of respondents, as herein alleged, were and are all to the prejudice and injury of the public and of respondents' competitors and constituted, and now constitute, unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT XII

Alleging violations of the Truth in Lending Act, and the implementing regulation promulgated thereunder, and of the Federal Trade Commission Act, as amended, the allegations of Paragraphs Two and Three hereof are incorporated by reference herein as if fully set forth verbatim.

PAR. 47. In the ordinary course and conduct of their business, as aforesaid, respondents regularly extend, and for some time in the past have regularly extended, consumer credit as "consumer credit" is defined in Regulation Z, the implementing regulation of the Truth in Lending Act, duly promulgated by the Board of Governors of the Federal Reserve System.

PAR. 48. Subsequent to July 1, 1969, respondents, in the ordinary course and conduct of their business, as aforesaid, and in connection with their credit sales, as "credit sale" is defined in Regulation Z, have caused, and are now causing, customers to execute binding "retail installment credit agreements," hereinafter referred to as the "credit agreement," for the purchase of respondents' goods and services. Said agreements constitute the only disclosure of consumer credit terms made to customers before a transaction is consummated.

PAR. 49. In connection with extensions of credit, respondents make disclosures to consumers describing the credit terms of their agreements and consumers' accounts. Said disclosures include, but are not limited to, disclosure that the finance charges will be computed by a periodic rate and disclosure of the annual percentage rate of such charges. Furthermore, in connection with their extensions of credit, respondents have caused to be delivered, and are delivering, to their customers, periodic billing statements. Based upon the foregoing, respondents profess to be extending open end credit.

PAR. 50. However, in further connection with their extensions of credit, respondents:

1. Fail to disclose, before the first transaction is made on the account, the minimum payment which will be required on future purchases.
2. Require customers to execute a new retail credit agreement for each subsequent purchase made on the account.
3. Require that under certain circumstances co-signers be obtained before additional purchases can be made.
4. Reverify as a matter of course the credit status of consumers with third parties before delivering merchandise purchased subsequent to the first sale.

PAR. 51. For the reasons set forth in Paragraph Fifty, and for other reasons not specifically set forth herein, respondents are not extending consumer credit on an account pursuant to a plan under which the respondents permit consumers to make repetitive transactions on a revolving basis, and are, therefore, extending other than open end credit.

PAR. 52. By and through the use of the aforementioned credit agreement, respondents:

1. Fail to make the required disclosures clearly, conspicuously, and in meaningful sequence, as prescribed by Section 226.6(a) of Regulation Z.
2. Fail to make the disclosures required by Section 226.8 of Regulation Z prior to the time the transaction is consummated either on:

(a) the note or other instrument evidencing the obligation on the same side of the page and above or adjacent to the place for the customer's signature; or

(b) one side of the separate statement which identifies the transaction as required by Section 226.8(a) of Regulation Z.

3. Fail to use the term "cash price" to describe the cash price, as

defined in Section 226.2(n) of Regulation Z, of the property purchased, as prescribed by Section 226.8(c)(1) of Regulation Z.

4. Fail to use the term "cash downpayment" to describe the downpayment in money made in connection with the credit sale as prescribed by Section 226.8(c)(2) of Regulation Z.

5. Fail to use the term "unpaid balance of cash price" to describe the difference between the cash price and the total downpayment, as prescribed by Section 226.8(c)(3) of Regulation Z.

6. Fail to use the term "unpaid balance" to describe the sum of the unpaid balance of cash price and all other charges which are included in the amount financed, but which are not a part of the finance charge, as prescribed by Section 226.8(c)(5) of Regulation Z.

7. Fail to use the term "amount financed" to describe the amount of credit of which the customer will have actual use determined in accordance with (c)(7) of Section 226.8 of Regulation Z, as required by Section 226.8(c)(7) of Regulation Z.

8. Fail to determine the sum of all charges incident to or as a condition of the extension of credit as required by Section 226.4 of Regulation Z and to disclose that sum, with a description of each amount included, using the term "finance charge" as required by Section 226.8(c)(8)(i) of Regulation Z and also fail to print this term more conspicuously than other terminology as required by Section 226.6(a) of Regulation Z.

9. Fail to disclose the sum of: the cash price, all charges which are included in the amount financed but which are not part of the finance charge, and the finance charge, and to describe that sum as the "deferred payment price," as required by Section 226.8(c)(8)(ii) of Regulation Z.

10. Fail to disclose the annual percentage rate, computed in accordance with Section 226.5 of Regulation Z, as required by Section 226.8(b)(2) of Regulation Z and to print that term more conspicuously than other terminology, as required by Section 226.6(a) of Regulation Z.

11. Fail to disclose the number, amounts and due dates or periods of payments scheduled to repay the indebtedness, and the sum of such payments, and to describe that sum as the "total of payments," as prescribed by Section 226.8(b)(3) of Regulation Z.

12. Fail to identify the amount or the method of computing the amount of any default, delinquency or similar charge payable in the event of late payments, as required by Section 226.8(b)(4) of Regulation Z.

13. Fail to disclose the method of computing any unearned

portion of the finance charge in the event of prepayment of the obligation, as required by Section 226.8(b)(7) of Regulation Z.

PAR. 53. Pursuant to Section 103(q) of the Truth in Lending Act, respondents' aforesaid failures to comply with the provisions of Regulation Z constitute violations of that Act and, pursuant to Section 108 thereof, respondents have thereby violated the Federal Trade Commission Act.

DECISION AND ORDER

The Commission having heretofore issued its complaint charging the respondents named in the caption hereof with violation of Section 5 of the Federal Trade Commission Act, as amended, and of the Truth in Lending Act and the implementing regulation promulgated thereunder, and the respondents having been served with a copy of that complaint, together with a notice of contemplated relief; and

The respondents, their attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter withdrawn this matter from adjudication in accordance with Section 3.25(c) of its Rules; and

The Commission having considered the matter and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 3.25(f) of its Rules, the Commission hereby makes the following jurisdictional findings and enters the following order:

1. Respondent Royal Furniture Co., Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located at 2936 Third Ave., Bronx, New York.

Respondent Milton Landes is an officer of said corporation. He formulates, directs, and controls the policies, acts and practices of said corporation, and his address is the same as that of said corporate respondent.

2. The Federal Trade Commission has jurisdiction of the subject

matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER I

A. *It is ordered,* That respondents, Royal Furniture Co., Inc., a corporation, its successors and assigns, and its officers, and Milton Landes, individually and as an officer of said corporation, and respondents' agents, representatives, and employees, directly or through any corporation, subsidiary, division or any other device, in connection with the purchasing, advertising, offering for sale, sale and distribution of furniture or other merchandise in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

1. Representing, directly or by implication, that respondents' terms of credit are lenient, including but not limited to representations that respondents offer "easy credit" or "instant credit" or that customers can arrange their own downpayments.
2. Failing to disclose conspicuously, in close conjunction with every mention of the availability of credit and credit terms in respondents' advertising, and in a manner appropriate to the media used, that co-signers may be required of persons whose credit ratings do not meet respondents' standards for credit accounts if respondents, in the course of their business, ever require co-signers.
3. Failing to offer to refund any consumer deposit placed towards purchases at the time the consumer's credit agreement for a purchase or credit account is disapproved and failing to make such refund within seven (7) business days from the request for such refund.
4. Failing to provide any consumer whose credit account or purchase is subject to credit approval with the following information, at the time the credit agreement is signed, in at least 12 point type:

IMPORTANT!

PLEASE READ THIS BEFORE YOU SIGN!

This contract will be checked by our credit department before we will deliver anything. Maybe they won't approve it. If they don't, we may ask you for a bigger downpayment. Or for bigger monthly payments. Or for one or more added signatures by relatives or friends (called co-signers) who'll promise to pay if you don't.

If you don't agree with those changes, you can cancel your order. As soon as you do that, we'll refund your downpayment.

Royal Furniture Co.

5. Unilaterally, and without the consumer's written consent, changing the terms of any credit agreement with a consumer after the consummation of the credit agreement including but not limited to requiring a larger deposit, co-signers, or purchase of less expensive merchandise. The consumer's right to give written consent can not be waived.

6. Using any collection or dunning letter which simulates a telegram or using any other methods or forms or types of communications which misrepresent the nature, import or urgency of any communication.

7. Representing to any consumer or co-signer against whom legal proceedings have been commenced, directly or by implication, that the account has been adjusted or such suits discontinued, unless:

(a) Within seven (7) business days of making an adjustment with such consumer or co-signer, respondents discontinue the legal proceedings by filing, or causing to be filed, with the court a notice of discontinuance or notice of settlement in the form required by the court.

(b) Within ten (10) business days from making such adjustment respondents send a copy of the papers required to be filed with the court in Order I(A)(7)(a) herein to the consumer and/or co-signer involved and, where applicable, to counsel representing the consumer and/or co-signer.

8. In the course of collecting a debt communicating or threatening to communicate with the consumer's employer or any agent of the employer or any other person not liable for the debt other than the spouse or attorney of the consumer or threatening repossession, wage garnishment, or other extraordinary measures, except:

(1) Inquiry to locate a consumer whose whereabouts are genuinely unknown to the creditor; and/or

(2) Inquiry to determine the nature and extent of a consumer's wages or property;

(3) Communication with credit bureaus to the extent permitted by the Fair Credit Billing Act, 15 U.S.C. 1666, and regulations promulgated thereunder.

Provided that, in these instances, no specific mention is made of the alleged indebtedness, except as permitted by the Fair Credit Billing Act, 15 U.S.C. 1666, and regulations promulgated thereunder.

9. Misrepresenting directly or by implication that respondents or

their representatives are New York City marshals, sheriffs, attorneys or any other state or local official.

10. Misrepresenting directly or by implication the debt collection activities that respondents or their representatives are engaging in or will engage in, including but not limited to threats of immediate repossession or wage garnishment prior to obtaining judgment.

11. Failing, at all times subsequent to the effective date of this order, to maintain complete records of all notices required by Order I(A) during the immediately preceding three-year period.

12. Failing to furnish to each customer who purchases any merchandise exceeding $50 in cost, and to each customer upon the opening of a credit or charge account, a booklet containing clear disclosures, in language which is easily understandable to such customers, describing their rights and obligations in respect to respondents': (1) warranties and guarantees; (2) refund policies, including the procedures established by Order I(A)(3), I(B)(1)(b), (c), (d) and (e); (3) delivery terms; (4) procedures for repair or replacement of non-conforming, defective or damaged merchandise, including the procedures established by Order I(B); and any other rights provided for in this order and any other material information. Such disclosures shall clearly delineate the conditions which customers must comply with in order to avail themselves of any procedure established by this order or by respondents. The booklet required herein shall be submitted for approval with the initial compliance report required by Order III(F).

13. Failing to disclose, orally and in writing, to each customer who purchases merchandise exceeding $50 in cost, and to each customer upon the opening of a credit or charge account, that the booklet required by Order I(A)(12) above is available and will be given to each such customer. Said written notice shall be given to such customers at the time of execution of their sales or credit agreements and shall contain the following language:

NOTICE TO CUSTOMER

BE SURE TO GET OUR BOOKLET!

Be sure to get our booklet that tells you about your rights. It contains our warranty and shows you what to do if something is wrong with the items we deliver. Or if the item you bought needs fixing. How to get repairs and replacements from us. Or how to get a refund.

Take the booklet home and study it carefully. Keep it handy for future reference.

14. Failing to display prominently and conspicuously the language required by Order I(A)(13) above in signs posted at four or more locations in that portion of respondents' business premises

most frequented by prospective customers, and in each location where customers normally execute sales agreements, consumer credit documents, or other binding instruments. Such language shall be considered prominently and conspicuously displayed only if so positioned as to be easily observed and read by intended individuals.

15. Failing to provide in such booklet that customers may have other legal rights concerning their contracts in addition to those set out in the contract and booklet.

16. Failing to comply with all requirements, or to fulfill all of the obligations to customers, which are set forth in Paragraph B of this Order I, and to comply with all of the procedures and rights set forth in this booklet.

B. *It is further ordered,* That beginning the effective date of this order respondents shall cease and desist from failing to act in accordance with the following procedures:

1. As to complaints, written or oral, of damaged, defective, or non-conforming merchandise, made within thirty (30) days of actual delivery of such merchandise:

(a) Respondents shall investigate all such complaints within fourteen (14) days from the date of such request, except that if a service person cannot gain access to the merchandise for a scheduled service call, respondents shall have seven (7) days from that missed appointment in which to investigate the complaint.

(b) Respondents shall repair to mint condition or make replacement or offer to make full refund of the purchase price of damaged, defective or non-conforming merchandise within a reasonable time not to exceed thirty-one (31) days from the date of complaint, unless: (1) such merchandise was sold "as is," and the notice requirements of Order I(B)(3) were complied with; or (2) the damage or defect in the merchandise was caused by the customer or another while the merchandise was in the customer's possession or control. Whenever respondents for either of the above reasons refuse a customer's request to repair or replace merchandise or to refund the purchase price thereof, respondents shall forthwith notify the customer in writing within the aforementioned thirty-one (31) day period of the specific reasons for the refusal and shall advise the customer of the customer's right to submit any dispute arising out of such refusal to a court of law including small claims court.

(c) If the repair or replacement of such damaged, defective or non-conforming merchandise is unsatisfactory to the consumer, respondents shall cancel all applicable contract provisions with a full refund within seven (7) business days from receipt of the customer's request for cancellation. Whenever respondents for valid reasons refuse a customer's cancellation and refund request pursuant to this section, respondents shall within seven (7) business days from receipt of said request notify the customer in writing of the specific reasons for the refusal and shall advise the customer of the customer's right to submit any dispute arising out of such refusal to a court of law including small claims court.

(d) If the investigation, repair, or replacement cannot be completed within the time specified by Paragraph B, subparts 1(a) and 1(b) of this Order I, respondents shall make diligent efforts to notify the customer orally and shall notify the customer in writing immediately upon ascertaining that respondents are unable to make timely performance, and shall, at the customer's option cancel all applicable contract provisions with a full refund within seven (7) business days from the date set for completion. In no event shall respondents' notice of inability to make timely performance be given to the customer after the last day set out for performance in Paragraph B, subparts 1(a) and 1(b) of this Order I.

(e) Respondents may refund in full the actual purchase price of the merchandise if repair is not commercially practicable and respondents are unable to provide replacement.

2. For purposes of the time limitations contained in Paragraph B of this Order I, customers may at any time give their written consent for an extension of respondents' time for performance. Such written consent shall set forth a date certain which shall be a date by which respondents actually expect to complete performance. No rights accruing from the provisions contained in this Order I shall be affected by such extension.

3. The provisions of Paragraph B of this Order I shall not apply to merchandise sold "as is," *provided, however,* that when merchandise is sold "as is" respondents shall provide the following information conspicuously on the face of the sales contract, invoice and receipt for merchandise:

WARNING — "AS IS" SALE.

NO WARRANTY.

This item may need repairs or replacements. Since it is sold "as is" without any warranty, you'll have to pay for them yourself. No matter what you've been told, we won't pay or return your money.

4. For purposes of the provisions of Paragraph B of this Order I,

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non-conforming merchandise shall include, but not be limited to, merchandise which, when delivered, is worn in appearance.

5. Respondents shall not sell merchandise without the implied warranty of merchantability, or with any disclaimer or limitation of such implied warranty, except that respondents may sell merchandise which is clearly designated "as is."

6. The investigation, pick-up and delivery of repair or replacement merchandise within the provisions of Paragraph B of this Order I shall be at no additional cost to the consumer.

7. No rights of consumers or co-signers conferred by state or local statutory law or by the common law shall be affected by the provisions and rights contained herein.

C. *It is further ordered,* That whenever a customer has sought the relief contained in Paragraph B of this Order I, or has advised respondents of the discontinuance of payment on the ground that respondents failed to deliver merchandise, to replace non-conforming merchandise, to repair or replace defective or damaged merchandise, or to make any refund to which a customer is entitled by reason of this order, or otherwise, that respondents desist from any action to collect the amount owed or any part thereof other than mailing a routine statement of account in regard to such merchandise and to desist from giving any adverse information to any credit reporting agency, unless respondents have conducted a thorough investigation of such complaint and made a written reply to the customer, stating whether respondents have concluded that such grievance is justified or unjustified, with reasons in support thereof and what action will be taken.

D. *It is further ordered,* That before any action is taken to collect an amount due from a customer, other than the mailing of a routine statement of account, or before any adverse information is sent to a credit reporting agency, respondents shall ascertain that they are not engaged in a dispute with said customer relating to the quality of the merchandise, or its replacement, condition or repair and, if so involved, verify that respondents have investigated and found the grievance to be unjustified and have so advised the customer, in accordance with the provisions of Paragraph C of this Order I.

E. Order provisions C and D of Order I shall be deemed modified in the event that respondents extend open end credit to the extent that order provisions C and D of Order I are inconsistent with the Fair Credit Billing Act and the regulations promulgated thereunder.

F. *It is further ordered,* That respondents shall, at all times subsequent to the effective date of this order, maintain, and produce for inspection and copying on reasonable demand by the Federal Trade Commission or its representatives, complete business records relating to the manner and form of their continuing compliance with this order during the immediately preceding three-year period, such records to include: (1) all refund, repair or replacement requests sent to respondents by customers; (2) all other grievance letters and documents received from customers; (3) adequate records to disclose the facts pertaining to the receipt, handling and disposition of each and every communication from a customer, oral or written, requesting cancellation, refund, replacement or repair; (4) all investigation reports concerning such grievances; and (5) all records pertaining to those customers to whom any collection or dunning notices have been sent.

Order II

It is further ordered, That respondent Royal Furniture Co., Inc., a corporation, its successors and assigns, and its officer, Milton Landes, individually and as an officer of said corporation, and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division or any other device, in connection with any extension of consumer credit, or any advertisement to aid, promote, or assist directly or indirectly any extension of consumer credit, as "consumer credit" and "advertisement" are defined in Regulation Z (12 CFR 226) of the Truth in Lending Act (Pub. Law 90-321, 15 U.S.C. 1601, *et seq.*) do forthwith cease and desist from:

1. Failing to make the required disclosures clearly, conspicuously, and in meaningful sequence, as prescribed by Section 226.6(a) of Regulation Z.
2. Failing to make all the required disclosures prior to the consummation of the transaction, in accordance with Section 226.8(a) of Regulation Z, either on:

(a) the note or other instrument evidencing the obligation on the same side of the page and above or adjacent to the place for the consumer's signature; or

(b) on one side of a separate statement which identifies the transaction.

3. Failing to use the term "cash downpayment" to describe the downpayment in money made in connection with the credit sale as prescribed by Section 226.8(c)(2) of Regulation Z.
4. Failing to use the term "cash price" to describe the cash price,

as defined in Section 226.2(n) of Regulation Z, of the property purchased, as prescribed by Section 226.8(c)(1) of Regulation Z.

5. Failing to use the term "unpaid balance of cash price" to describe the difference between the cash price and the total downpayment, as prescribed by Section 226.8(c)(3) of Regulation Z.

6. Failing to use the term "unpaid balance" to describe the sum of the unpaid balance of cash price and all other charges which are included in the amount financed, but which are not part of the finance charge, as prescribed by Section 226.8(c)(5) of Regulation Z.

7. Failing to use the term "amount financed" to describe the amount of credit of which the customer will have actual use determined in accordance with Section (c)(7) of Section 226.8 of Regulation Z.

8. Failing to determine the sum of all charges incident to or as a condition of the extension of credit as required by Section 226.4 of Regulation Z and to disclose that sum, with a description of each amount included, using the term "finance charge," as required by Section 226.8(c)(8)(i) of Regulation Z and also to print this term more conspicuously than other terminology as required by Section 226.6(a) of Regulation Z.

9. Failing to disclose the sum of the cash price, all charges which are included in the amount financed but which are not part of the finance charge, and the finance charge, and to describe that sum as that "deferred payment price," as required by Section 226.8(c)(8)(ii) of Regulation Z.

10. Failing to disclose the annual percentage rate, computed in accordance with Section 226.5 of Regulation Z, as required by Section 226.8(b)(2) of Regulation Z and to print that term more conspicuously than other terminology, as required by Section 226.6(a) of Regulation Z.

11. Failing to disclose the number, amounts and due dates or periods of payments scheduled to repay the indebtedness, and the sum of such payments, and to describe that sum as the "total of payments," as prescribed by Section 226.8(b)(3) of Regulation Z.

12. Failing to identify the amount or the method of computing the amount of any default, delinquency or similar charge payable in the event of late payments, as required by Section 226.8(b)(4) of Regulation Z.

13. Failing to disclose the method of computing any unearned portion of the finance charge in the event of prepayment of the obligation, as required by Section 226.8(b)(7) of Regulation Z.

14. Failing, in any consumer credit transaction or advertisement, to make all disclosures determined in accordance with Sections 226.4

and 226.5 of Regulation Z, in the manner, form and amount required by Sections 226.6, 226.7, 226.8, 226.9 and 226.10 of Regulation Z.

ORDER III

A. *It is further ordered,* That respondents prominently display the following notice in two or more locations in that portion of respondents' business premises most frequented by prospective customers, and in each location where customers normally sign consumer credit documents or other binding instruments. Such notice shall be considered prominently displayed only if so positioned as to be easily observed and read by the intended individuals:

NOTICE TO OUR CREDIT CUSTOMERS

If you're going to pay in installments, ask for a statement that shows exactly how much you're going to pay. The law says you must be given that statement before you sign any papers. *Don't sign before you've read the statement.* If there's anything you don't understand, please ask us.

B. *It is further ordered,* That respondents deliver a copy of this order to cease and desist to all operating divisions and to all present and future personnel of respondents engaged in consummation of any consumer credit transaction or in any aspect of preparation, creation, or placing of advertising, and to all personnel of respondents responsible for the sale or offering for sale of all products covered by this order, and that respondents secure a signed statement acknowledging receipt of said order from each such person.

C. *It is further ordered,* That respondents shall maintain, and produce for inspection and copying on reasonable demand by the Federal Trade Commission or its representatives, for at least a one (1) year period, following the effective date of this order, copies of all advertisements, including newspapers, radio and television advertising, direct mail and instore solicitation literature, and any other such promotional material utilized in the advertising, promotion or sale of merchandise.

D. *It is further ordered,* That respondents notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of the order.

E. *It is further ordered,* That the individual respondent named herein promptly notify the Commission of the discontinuance of his present business or employment and of his affiliation with a new business or employment. In addition, for a period of ten years from the effective date of this order, the respondent shall promptly notify the Commission of each affiliation with a new business or employment. Each such notice shall include the respondent's new business address and a statement of the nature of the business or employment in which the respondent is newly engaged as well as a description of respondent's duties and responsibilities in connection with the business or employment. The expiration of the notice provision of this paragraph shall not affect any other obligation arising under this order.

F. *It is further ordered,* That the respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

IN THE MATTER OF

FEDERATED DEPARTMENT STORES, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2958. Complaint, April 2, 1979 — Decision, April 2, 1979

This consent order, among other things, requires a Cincinnati, Ohio operator of retail department stores to cease entering into or enforcing agreements which grant the firm the right to exclude certain tenants from shopping centers; control tenants' advertising, goods and prices; or otherwise restrict competition.

Appearances

For the Commission: *David I. Keniry.*

For the respondent: *G. Duane Vieth, Arnold & Porter,* Washington, D.C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, (15 U.S.C. 41, *et seq.*) and by virture of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that the corporation named as respondent in the caption hereof, and more particularly designated and described hereinafter, has violated and is now violating the provisions of Section 5 of the Federal Trade Commission Act, as amended, and it appearing to the Commission that a proceeding by it in respect thereof is in the public interest, hereby issues its complaint, stating the following:

PARAGRAPH 1. For the purpose of this complaint the following definitions shall apply:

a. The term "respondent" refers to Federated and its operating divisions, officers, agents, representatives, employees, successors, and assigns.

b. The term "shopping center" refers to a planned development of retail outlets in the United States of America, developed and managed as a unit in relation to a trade area which the development is intended to serve and containing (1) a total floor area designed for retail occupancy of 250,000 square feet or more, of which at least 50,000 square feet is for occupancy by tenants other than respondent,

(2) at least two tenants other than respondent, (3) at least one major tenant, and (4) on-site parking.

c. The term "tenant" refers to any occupant or potential occupant of retail space in a shopping center, which occupancy is for the sale of merchandise or services to the public, whether said occupant leases or owns said space, but the term does not refer to any occupant or potential occupant of space within respondent's store or other areas operated by respondent, which occupant is to operate a department for respondent pursuant to a lease or license from respondent.

d. The term "major tenant" refers to a tenant providing primary drawing power in a shopping center. A tenant occupying 50,000 square feet or more shall be presumed to provide primary drawing power.

e. The term "trading area" means the geographical bounds within which tenants of a shopping center derive the predominance of their customers.

f. The term "Boston market" means the Boston Massachusetts Standard Metropolitan Statistical Area as is defined in the Bureau of the Budget Publication, "Standard Metropolitan Statistical Areas, 1972."

PAR. 2. Respondent Federated Department Stores, Inc. (hereinafter referred to as "Federated") is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 222 West Seventh St., Cincinnati, Ohio. Respondent Federated operates and controls its 19 divisions from its principal office and place of business.

In fiscal 1975, Federated's total sales volume was approximately 3.7 billion dollars. Department stores sales accounted for approximately 2.7 billion dollars or 74% of Federated's total sales volume.

Federated and fourteen of its nineteen divisions are engaged in the operation of retail department stores (Abraham & Straus, Bloomingdale's, Bullock's South, Bullock's North, Burdine's, Filene's, Foley's, Goldsmith's, Lazarus, Levy's, Milwaukee Boston Store, Rike's Sanger-Harris, and Shillito's). In addition, Federated's I. Magin & Company division operates twenty-two specialty stores.

In 1975, Federated's 15 department or specialty store divisions operated approximately 141 department or specialty stores with cumulative floor space of approximately 30 million square feet.

In the Boston, Massachusetts metropolitan area, one of the thirteen metropolitan areas in which Federated operates department stores, Federated owns, operates, directs and controls the Filene's department store chain, a division with its principal office and place of business at 426 Washington St., Boston, Massachusetts. Filene's is one of the leading department stores in New England. Federated operates six Filene's department stores in the Boston market encompassing approximately 1.3 million square feet of floor square.

Five of Filene's six department stores in the Boston market are located in the following shopping centers:

a. North Shore Shopping Center
Peabody, Massachusetts

b. South Shore Plaza
Braintree, Massachusetts

c. Burlington Mall
Burlington, Massachusetts

d. Natick Mall
Natick, Massachusetts

e. Chestnut Hill Mall
Chestnut Hill, Massachusetts

Federated also operates a Filene's department store in Boston's central business district and two limited-line Filene's stores in suburban Belmont and Wellesley. Federated operates three Filene's department stores in shopping centers outside of the Boston market, at the following locations:

a. Cape Cod Mall
Hyannis, Massachusetts
b. Worcester Center
Worcester, Massachusetts
c. Warwick Mall
Warwick, Rhode Island

PAR. 3. In the course and conduct of its business, Federated has engaged and is now engaged in acts and practices in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended. Respondent purchases for resale a variety of consumer products from numerous suppliers located throughout the United States. Respondent causes these products, when purchased by it, to be transported from the place of manufacture or purchase to its warehouses and retail department stores located in Massachusetts, Texas, Florida, California and other states. Such products have been and are advertised for sale by respondent in newspapers and direct mailings circulated among and between the several states of the nation and by the interstate transmission of promotional sales messages by means of the various broadcast media.

PAR. 4. The movement of population, and particularly the higher income segment of the population, from the central city to the suburbs, has precipitated the growth of shopping centers in suburban areas. In 1960, there were approximately 4,500 shopping centers in the United States; their number now exceeds 14,000 and is projected to reach 20,000 by 1980. In 1970, retail sales in shopping centers amounted to $118 billion and accounted for 32.2% of all United States retail sales. Retail sales in shopping centers are projected to reach $200 billion by 1980.

Shopping centers reproduce to a substantial extent the retail facilities once available only in downtown business districts, and are displacing and replacing the central downtown business district as primary outlets for retail distribution of goods and services. Department store operators, including respondent herein, have recognized the potential business opportunities presented by the expanding suburban markets and have, in recent years, established themselves in shopping centers.

PAR. 5. Except to the extent that competition has been hindered, frustrated and eliminated as set forth in this complaint, respondent, in the course and conduct of its business of offering for sale and selling household goods, home furnishings, apparel and diverse other consumer goods, has been and is in substantial competition with other corporations, individuals and partnerships in the retail sale of the same or comparable brands of merchandise carried and sold by respondent.

PAR. 6. Federated, in its capacity as a tenant, has entered into agreements with developers and other major tenants at various shopping centers throughout the country, which agreements contain various kinds of restrictive covenants and provisions hereinafter more fully described.

PAR. 7. In the course and conduct of its business, Federated is and has been engaged in unfair methods of competition and unfair acts and practices in or affecting commerce, in that it has included, caused the inclusion of, or enforced or caused the enforcement of, restrictive agreements, provisions and covenants which lessen, prevent and foreclose competition in the resale and distribution at retail of goods and services.

PAR. 8. The inclusion or enforcement of the aforesaid covenants and provisions, and the rights, powers and privileges conferred thereby, have had and continue to have the tendency to restrain

a. Allowing Federated to choose its competitors and to exclude actual and potential competitors;

b. Hindering or discouraging certain types of retail operations, including discount stores;

c. Excluding tenants from shopping centers; and

d. Restricting and hindering developers in their choice of tenants in shopping centers.

PAR. 9. The inclusion or enforcement of the provisions and covenants referred to above constitute an unfair method of competition and unfair acts and practices in or affecting commerce within the intent and meaning of Section 5 of the Federal Trade Commission Act, as amended.

Commissioner Pitofsky did not participate.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Boston Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act, as amended; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint; and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Federated Department Stores, Inc. is a corporation organized, existing and doing business under and by virtue of

the laws of the State of Delaware, with its principal office and place of business located at 222 West Seventh St., Cincinnati, Ohio.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

I.

For the purposes of this order the following definitions shall apply:

(a) The term "respondent" refers to Federated and its operating divisions, officers, agents, representatives, employees, successors, and assigns.

(b) The term "shopping center" refers to a planned development of retail outlets in the United States of America, developed and managed as a unit in relation to a trade area which the development is intended to serve and containing (1) a total floor area designed for retail occupancy of 250,000 square feet or more, of which at least 50,000 square feet is for occupancy by tenants other than respondent, (2) at least two tenants other than respondent, (3) at least one major tenant, and (4) on-site parking.

(c) The term "tenant" refers to any occupant or potential occupant of retail space in a shopping center, which occupancy is for the sale of merchandise or services to the public, whether said occupant leases or owns said space, but the term does not refer to any occupant or potential occupant of space within respondent's store or other areas operated by respondent, which occupant is to operate a department for respondent pursuant to a lease or license from respondent.

(d) The term "major tenant" refers to a tenant providing primary drawing power in a shopping center. A tenant occupying 50,000 square feet or more shall be presumed to provide primary drawing power.

II.

It is ordered, That respondent, in its capacity as a tenant in a shopping center, cease and desist from obtaining, making, carrying out or enforcing, directly or indirectly, any agreement or provision of an agreement which:

1. Grants respondent the right to approve or disapprove the entry into a shopping center of any other tenant;

2. Prohibits the admission into a shopping center of any particu-

lar tenant or class of tenants, including, without limitation, for purposes of illustration:

(a) other department stores;

(b) junior department stores;

(c) discount stores; or

(d) catalogue stores;

3. Limits the types or brands of merchandise or services which any other tenant in a shopping center may offer for sale;

4. Specifies that any other tenant in a shopping center shall or shall not sell its merchandise or services at any particular price or within any range of prices;

5. Grants respondent the right to approve or disapprove the location in a shopping center of any other tenant;

6. Specifies or prohibits the content of any advertising by any other tenant or grants respondent the right to approve or disapprove the content of any advertising by any other tenant;

7. Grants respondent the right to approve or disapprove the amount of floor space that any other tenant may occupy in a shopping center; or

8. Prohibits the owner or occupant of real property adjoining, abutting or adjacent to a shopping center in which respondent is a tenant from using such property for the sale of merchandise or services similar or identical to the merchandise or services sold in the shopping center; *provided. however,* that nothing in this paragraph shall apply to an agreement or provision thereof which affirmatively prescribes particular land uses or zoning for any real property.

III.

A. *It is further ordered,* That this order shall not prohibit respondent from negotiating to include, including, carrying out or enforcing any agreement or provision in any agreement relating to respondent's occupancy, or proposed occupancy, of space in a shopping center, which (1) identify in designated buildings respondent and those major tenants which have entered, or which are to contemporaneously enter or which the developer or landlord represents in writing have stated an intention to enter, into agreements for occupying space in the shopping center, (2) recite that respondent and such major tenants have contracted or shall contract with the developer or landlord to maintain and operate their stores for a specified term, not to exceed 25 years, in such designated buildings, and (3) provide for respondent's right to cancel, terminate or modify its agreement for occupancy if such major tenants do not occupy such designated buildings or do not maintain and operate their stores for the specified term.

B. *It is further ordered,* That this order shall not prohibit respondent from negotiating to include, including, carrying out or enforcing an agreement or provision in any agreement which:

1. Requires that in selecting other tenants in a shopping center the developer shall select businesses which are financially sound and which will in the aggregate provide a balanced and diversified grouping of retail stores, merchandise and services in the shopping center;

2. Requires that specified standards of appearance, signs, maintenance, heating, air conditioning, lighting and housekeeping be maintained in a shopping center;

3. Establishes a layout of a shopping center which layout may designate: (a) respondent's store and stores which are to be occupied by other major tenants; (b) the location, size and height of all structures (including any structure that is to be occupied by only one tenant) but not the amount of floor space that any other tenant may occupy in the shopping center; (c) the minimum floor space to be occupied by respondent and by major tenants; (d) uses of all structures to be used for purposes other than the retail sale of merchandise or services to the public; (e) parking ratios, parking areas (including stall sizes and arrangement), roadways, utilities, entrances, exits, walkways, malls, landscaped areas and other common areas; and (f) expansion areas and may within such areas establish a layout incorporating items (a) through (e) of this subsection 3;

4. Requires that any change or expansion of a shopping center not provided for in the initial layout:

(a) shall not interfere with efficient automobile and pedestrian traffic flow into and out of the shopping center and between respondent's store and perimeter and access roads, parking areas, malls and other common areas of the shopping center;

(b) shall not interfere with the efficient operation of respondent's store, including its utilities, and shall not interfere with the visibility of its signs from within the shopping center or from public highways adjacent thereto;

(c) shall not result in a change of (i) the shopping center's parking ratio, (ii) the location of a number of parking spaces reasonably accessible to respondent's store, (iii) the entrances and exits to and from respondent's store and any malls, and (iv) those parking area mall entrances and exits which substantially serve respondent's store; or

(d) shall be accomplished only after any and all covenants, obligations and standards (for example, construction, architecture, operation, maintenance, repair, alteration, parking ratio, and easements) of the shopping center, exclusive of the expansion area (i) shall be made applicable to the expansion area and (ii) shall be made prior in right to and all mortgages, deeds of trust, liens, encumbrances, and restrictions applicable to the expansion area, and (iii) shall be made prior in right to any and all other covenants, obligations and standards applicable to the expansion area;

5. Prohibits occupancy of space in a shopping center by types of tenants that create undue noise, litter or odor;

6. Permits respondent to establish reasonable categories of tenants from which the developer or landlord of a shopping center may select tenants to be located in the area immediately proximate to respondent's store; *provided,* that such categories shall not include specification of (a) trade names, (b) store names, (c) trademarks, brands or particular lines of merchandise, or (d) identity of particular retailers, including the listing of particular retailers as examples of a category; *provided,* that such area shall not exceed the greater of (i) 150 lineal feet from respondent's store on each level of the center, or (ii) 20% of the total lineal mall front footage, exclusive of respondent's store, on each level of the center;

7. Prohibits occupancy of space in a shopping center by clearly objectionable types of tenants, including, for purposes of illustration, establishments selling or exhibiting pornographic materials;

8. Requires that any space designated for occupancy by a major tenant in the initial layout of the shopping center not be leased for occupancy by other than a major tenant, that any sub-division of such space for occupancy by more than one tenant not result in any tenant occupying less than 50,000 square feet of such space or that each successive occupancy of such space be for the sale of merchandise or services to the public;

9. Prohibits or establishes limitations on the location in the shopping center of commercial office buildings, hotels, motor inns, new and used automobile dealers or funeral parlors; or

10. Establishes reasonable limitations on the location in the shopping center of fast food outlets, grocery supermarkets or movie theaters.

IV.

It is further ordered, That respondent shall:

A. Within thirty (30) days after service of this order upon respondent, distribute a copy of this order to each of its directors, officers, and to each of its operating divisions;

B. Within thirty (30) days after service of this order upon respondent, notify each landlord of a shopping center in which respondent is a tenant, of this order by providing each landlord with a copy thereof by certified mail;

C. Within ninety (90) days after service of this order upon respondent, file with the Commission a report showing the manner and form in which it has complied and is complying with each and every specific provision of this order; and

D. Notify the Commission at least thirty (30) days prior to any proposed change in the respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which would affect compliance obligations arising out of the order.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

CRANE CO., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND CLAYTON ACTS

Docket C-2959. Complaint, April 5, 1979 — Decision, April 5, 1979

This consent order, among other things, requires a New York City manufacturer and seller of various products to cause the Medusa Corporation to divest itself completely of its Dixon, Ill. cement plant, together with whatever assets associated with the plant that may be necessary to maintain the facility as an effective competitor in the production and sale of portland cement. The order further prohibits respondents from acquiring the whole or part of the assets of any firm engaged in the production or sale of portland cement without prior Commission approval.

Appearances

For the Commission: *James S. Teborek* and *Bert L. Slonim.*

For the respondent: *Pro se.*

COMPLAINT

The Federal Trade Commission, having reason to believe that Thomas Mellon Evans ("T.M. Evans") presently influences the management of Crane Co. ("Crane"), H.K. Porter, Inc. ("Porter") and its subsidiary, Missouri Portland Cement Company ("MPC"), that Crane presently owns approximately forty-four (44%) percent of the shares of Medusa Corporation ("Medusa"), that Crane intends to tender for any and all of the outstanding shares of Medusa stock, that Crane's present ownership of Medusa capital stock, its acquisition of additional capital stock of Medusa, or the merger of Medusa with Crane violates or would violate individually or collectively, Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, pursuant to Section 11 of the Clayton Act, 15 U.S.C. 21, 5(b), of the Federal Trade Commission Act, as amended, 15 U.S.C. 45(b), stating its charges as follows:

I. Definitions

1. For the purpose of this complaint the following definitions shall apply:

a. "Portland cement" includes Types I through V of portland cement as specified by the American Society for Testing Materials. Neither masonry nor white cement is included.

b. "Chicago Metropolitan Area" ("CMA") refers to that area of the State of Illinois composed of the counties of Cook, DuPage, Lake, McHenry, Kane and Will, including any and all independent cities, towns, or other political units located therein.

c. "Peoria Metropolitan Area" ("PMA") refers to that area of the State of Illinois composed of the counties of Peoria, Woodford and Tazewell, including any and all independent cities, towns, or other political units located therein.

II. Crane Co.

2. Crane is a corporation organized and existing under the laws of the State of Illinois with its principal office at 300 Park Ave., New York.

3. Crane manufactures and sells a variety of products, including pollution control devices, plumbing and related building materials, aircraft systems and accessories, and various other products through its subsidiaries.

4. In its fiscal year ended December 31, 1977, Crane had total net sales of $1,113,000,000, with total assets of $836,895,000. Net income for 1977 totaled $66,171,000.

III. Thomas Mellon Evans and the H. K. Porter Company

5. Approximately 12% of Crane's shares are owned by its largest shareholder T.M. Evans. Another 3% or more is held directly or indirectly by T.M. Evans' three sons or by corporations, charitable or otherwise, controlled by T.M. Evans or of which T.M. Evans serves as officer or trustee.

6. Mr. T.M. Evans also owns approximately 62% of the shares of Porter, a corporation organized and existing under the laws of the State of Delaware with principal offices at 1500 Porter Building, Pittsburgh, Pa.

7. In 1977, Porter's net sales totaled $113,683,000, with net income for 1977 of approximately $10,277,000. Through its wholly-owned subsidiary, MPC, which it acquired in 1976, Porter is engaged in the manufacture of portland cement.

8. MPC is a corporation organized and existing under the laws of the State of Delaware with its principal offices at 7711 Carondelet Ave., St. Louis, Missouri. MPC produces portland cement at plants located in Missouri and in Illinois. MPC operates distribution terminals in the Chicago and Peoria Metropolitan Areas, Tennessee,

Kentucky, Nebraska, and Alabama. In 1977, MPC's net sales totaled $67,411,000, with net income of $2,476,000. MPC's total assets were valued at $81,073,000.

9. Mr. T.M. Evans serves as a Director and Chairman of the Board of Crane, Director and Chairman of the Executive Committee of Porter and, until August 18, 1978, as a Director of MPC. Mr. T.M. Evans' three sons have stock holdings and or managerial positions in Crane, Porter and/or MPC.

IV. Medusa Corporation

10. Medusa is a corporation organized and existing under the laws of the State of Ohio, with its principal office at 3615 Warrensville Center Road, Shaker Heights, Ohio.

11. Medusa produces and sells portland cement, brick, asphalt and a variety of other highway construction materials or aggregates. Medusa also engaged in highway safety construction and asphalt paving. In 1977, Medusa's total revenues were approximately $243,000,000 with an operating profit of $29,000,000.

12. Medusa produces portland cement at plants located in Georgia, Illinois, Michigan, Ohio and Pennsylvania and operates nine distribution teminals including two located in the Chicago Metropolitan Area. In 1977, Medusa's sales of portland cement exceeded $100,000,000.

V. Jurisdiction

13. At all times relevant herein MPC and Medusa have been engaged in the production and sale of portland cement in interstate commerce and MPC, Crane, and Medusa are engaged in commerce as "commerce" is defined in the Clayton Act, as amended, 15 U.S.C. 12, *et seq.* and each is a corporation whose business is in or affects commerce as "commerce" is defined in the Federal Trade Commission Act, as amended, 15 U.S.C. 41, *et seq.*

VI. The Initial Acquisition

14. On or about August 15, 1978, Crane acquired approximately 514,000 shares of Medusa's common stock thus increasing its holdings to approximately 600,000 shares or 20% of Medusa's outstanding shares.

VII. The Tender Offer

15. On or about September 28, 1978, Crane purchased an additional 700,000 shares of Medusa's common stock, approximately

24% of Medusa's outstanding shares, pursuant to a tender offer the terms of which are set forth in the Schedule 14D-1 filed by Crane with the Securities and Exchange Commission on or about September 5, 1978.

VIII. The Merger Agreement

16. On or about August 31, 1978, Crane and Medusa entered into an agreement in principle to merge upon the completion of Crane's tender offer. On or about November 14, 1978 Crane announced that it had abandoned its announced intention to merge with Medusa.

IX. The Exchange Offer

17. On or about November 14, 1978, Crane announced that it intended to make an exchange offer for any and all of the outstanding shares of Medusa stock where Crane would offer $10.00 in cash and $40.00 in principal amount of Crane's subordinated debentures for each Medusa share tendered.

X. Trade and Commerce

18. The relevant line of commerce is the manufacture and sale of portland cement.

19. A relevant section of the country or geographic market is the area of present competition between Medusa and MPC and various geographic markets thereof, including but not limited to CMA and PMA.

XI. Actual Competition

20. MPC and Medusa are and have been for many years actual competitors in the manufacture and sale of portland cement within certain geographic markets, including CMA and PMA.

XII. Effects; Violations Charged

21. The effect of T.M. Evans' stockholdings and managerial positions in Crane and Porter may be to substantially lessen competition or tend to create a monopoly or to constitute an unfair method of competition in violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

22. The effects of Crane's present holdings of Medusa's shares, and its pending tender offer for additional Medusa shares may be to substantially lessen competition or tend to create a monopoly in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18,

and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, in the following ways, among others:

(a) actual competition between MPC and Medusa in the manufacture and sale of portland cement may be eliminated;

(b) actual competition between competitors generally in the manufacture and sale of portland cement may be lessened;

(c) concentration in the manufacture and sale of portland cement may be increased and the possibilities for eventual deconcentration may be diminished;

(d) mergers or acquisitions between other portland cement producers may be fostered, thus causing a further substantial lessening of competition or tendency toward monopoly in the manufacture and sale of portland cement; and

(e) barriers to entry into the manufacture and sale of portland cement may be increased.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Chicago Regional office and the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act and the Clayton Act; and

The respondents, their attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint and waivers and other provisions as required by the Commission's Rules; and

The Commission having considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Crane Co. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois, with its office and principal place of business located at 300 Park Ave., in the City of New York, State of New York.

Respondent Thomas M. Evans is an individual whose business address is the same as that of Crane Co.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

It is ordered, That respondents — Crane Co., ("Crane") a corporation, its successors and assigns, and its officers and directors, and Thomas M. Evans, an individual, his successors and assigns — in connection with the acquisition by Crane, a corporation engaged in commerce as "commerce" is defined in the Clayton Act, as amended, 15 U.S.C. 12, *et seq.*, of stock in Medusa Corporation ("Medusa") a corporation engaged in commerce as "commerce" is defined by the Clayton Act, as amended, 15 U.S.C. 12, *et seq.*, which acquisition is in or affects commerce as "commerce" is defined in the Federal Trade Commission Act, as amended, 15 U.S.C. 41, *et seq.*:

I

Within fifteen (15) months from the date of service of the consent order upon respondents, and subject to the prior approval of the Federal Trade Commission, respondents shall cause Medusa's cement plant located at Dixon, Illinois and such other of Medusa's assets associated with that plant as may be necessary, so that the plant may operate as a going concern and effective competitor in the production and sale of portland cement.

II

It is further ordered, That respondents shall not cause or permit the destruction, removal or impairment of any of the assets to be divested in accordance with Paragraph I of the consent order except in the ordinary course and operation of Medusa's business and except for normal wear and tear.

III

It is further ordered, That if the divestiture of assets required by

Paragraph I of the consent order is to be accomplished by a spin-off, then:

(a) Respondents shall cause Medusa to transfer the assets to be divested to a new corporation, whose stock is wholly-owned by Medusa, and then Medusa shall distribute that stock to Medusa's shareholders in proportion to their ownership of Medusa stock. Crane shall promptly thereafter distribute its share of the stock of the newly created corporation either to Crane's shareholders in proportion to their ownership of Crane stock or through a public offering to be completed within three months.

(b) No person who is an officer, director or executive employee of Crane or Porter or who owns or controls directly or indirectly more than one (1) percent of the stock of Crane or Porter shall be an officer, director or executive employee of the new corporation.

(c) Neither Thomas M. Evans nor any other person who is an officer, director or executive employee of Crane shall own or control, directly or indirectly, more than one (1) percent of the stock of the new corporation.

(d) Any person who must sell or dispose of stock interest in Crane or H.K. Porter or the new corporation in order to comply with subparagraphs (b) or (c) shall do so within one hundred eighty (180) days after the date on which distribution of the stock of the new corporation is made to stockholders of Crane.

IV

It is further ordered, That for a period of five (5) years from the date of service of the consent order upon respondents, respondents shall cease and desist from acquiring directly or indirectly, by any device or through any corporation, subsidiary or otherwise:

(a) the whole or any part of the assets of any firm engaged in the production or sale of portland cement;

(b) any equity securities in excess of three (3) percent of the outstanding shares of such securities of any firm engaged directly or indirectly in the production or sale of portland cement, except that respondents shall be permitted to acquire Crane, Porter or Medusa stock without restriction;

without the prior approval of the Federal Trade Commission.

V

It is further ordered, That for any company in which respondents own securities pursuant to Paragraph IV of this order, respondents, their designees, agents, nominees, or representatives shall not seek or accept representation on the Board of Directors of such company.

VI

It is further ordered, That nothing in this consent order shall prevent Evans & Company, a registered securities broker-dealer, from trading in the securities of any firm engaged in the production or sale of portland cement in the ordinary course of its business for:

(a) those of its customers who are not affiliates or subsidiaries of respondents;
(b) respondents acquiring securities pursuant to paragraph IV.

VII

A. *It is further ordered,* That respondents distribute a copy of this order to all operating divisions of said corporation.

B. *It is further ordered,* That respondents notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

C. *It is further ordered,* That within sixty days and every sixty days thereafter until Medusa has divested absolutely the assets required by the consent order, respondents shall submit a detailed written report of their actions, plans and progress in complying with Paragraphs I, II and III of the consent order, and in fulfilling the objectives of these provisions.

D. *It is further ordered,* That annually on the anniversary date of the service of the consent order, for a period of five years, respondents shall submit a detailed written report of their actions in complying with Paragraphs IV and V of the consent order, and in fulfilling the objectives of these provisions.

IN THE MATTER OF

GAC CORPORATION, ET AL.

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2523. Decision, July 23, 1974 — Modifying Order, April 17, 1979

This order modifying an order to cease and desist issued on July 23, 1974, 39 FR 34021, 36960; 84 F.T.C. 163, requires the incorporation of the terms of the 1974 order within any GAC plan of reorganization under provisions of the Bankruptcy Act confirmed by the Bankruptcy Court. Upon such confirmation, the modified order requires the company to establish a $10,000,000 accrual Reserve Fund to be used to defray costs of building individual septic tanks or wells in the northern section of Golden Gates Estates, and to reimburse those whose land is found to be unsuitable for homesites. Because of GAC's poor financial condition, the company is only required to develop a portion of Golden Gates Estates, rather than the entire subdivision, as previously mandated; and is provided with additional time in which to fulfill its contractual obligations to land owners. The modified order further requires GAC to provide financial compensation or alternate homesites to those owning property in the area to be left undeveloped.

ORDER MODIFYING ORDER TO CEASE AND DESIST

The Commission on February 13, 1979, issued its order to show cause why this proceeding should not be reopened and its order of July 23, 1974 (hereafter sometimes referred to as "the Commission Order of 1974"), modified.

Respondents having filed an answer consenting to the proposed changes of the Commission Order of 1974, and the Commission having considered the comments filed by interested persons,

Now, therefore, it is hereby ordered, That the aforesaid order to cease and desist be, and it hereby is, modified in accordance with the show cause order subject to, and contingent upon, satisfaction of all of the following conditions:

(1) the incorporation of the terms of the Commission Order of 1974, as modified, within any plan of reorganization of the respondent confirmed by the Bankruptcy Court in the aforesaid Chapter X proceedings (hereafter referred to as the "plan of reorganization") such incorporation to be without any alterations, substitutions, changes or deletions of the Commission Order of 1974, as modified;

(2) the incorporation of an express provision within any plan of reorganization of the respondent confirmed by the Bankruptcy Court in the aforesaid Chapter X proceedings that the reorganized company which is created thereby shall be subject to the requirements of the Commission Order of 1974, as modified;

(3) the incorporation of an express provision within any plan of reorganization of the respondent, confirmed by the Bankruptcy Court in the aforesaid Chapter X proceedings, that the reorganized company shall stipulate and agree to the enforcement as provided by law, including, but not limited to, as provided under Section 45(1), Title 15, United States Code. Provided further that nothing contained in the order modifying the Commission Order of 1974, and no action taken by the Bankruptcy Court in the aforesaid Chapter X proceedings, shall in any way restrict the right of any lot purchaser or title holder who chooses to reject the alternatives provided in the Commission Order of 1974, as modified, from filing any claim he or she may otherwise have against the respondent in the aforesaid Chapter X proceedings; however, the acceptance of any of the alternatives provided shall act as a bar to the filing of any other claims relating to the same land of the lot purchaser or titleholder or the contract applicable thereto prior to confirmation of the plan of reorganization.

Upon full satisfaction of all of the above conditions, the Commission Order of 1974 shall be modified, without necessity of further action by the Commission, as follows:

Order

For purposes of this order the following definitions shall be applicable:

"Land" shall mean real property subdivided into parcels without any house or building constructed thereon, but shall not include anything defined below as "other real property."

"Other real property" shall mean a house or building constructed for residential purposes and the land upon which it is situated, including land upon which, pursuant to a purchase agreement or contract, a house or building is to be constructed within 12 months and with respect to which no consideration will pass to respondents until closing other than moneys held in escrow or a minimal earnest money deposit.

"Consumer" shall mean a natural person to whom respondents offer to sell or sell land or other real property; *provided, however,* that the term "consumer" shall not include a natural person who purchases land in a single transaction for a sum in excess of $50,000.

I.

As used in this section of the order, a requirement to cease and desist from representing or misrepresenting shall unless otherwise indicated, include representing or misrepresenting directly or by implication, and by any manner or means.

It is ordered, That respondents GAC Corporation, GAC Properties, Inc. and GAC Properties, Inc. of Arizona, corporations, and their officers, and their subsidiaries and the said subsidiaries' officers, and respondents' successors, assigns, agents, representatives and employees, directly or through any corporate or other device in connection with the advertising, offering for sale, or sale of land and other real property to consumers in commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. (a) Failing to disclose, clearly and conspicuously, in any written or oral invitation or other initial communication to consumers concerning any event or activity, including but not limited to dinner parties or other gatherings, contests, awards of free or low cost gifts or vacations, and sightseeing tours, or for any other goods or services, which invitation or communication is in any manner a part of a plan or procedure to sell land, the following statement:

The purpose of [the event or activity] is to attempt to sell you land presently undeveloped in [name of State in which land is located].

(b) (i) If the invitation or communication is in writing, such disclosure shall be in writing and shall be made clearly and conspicuously and in conjunction with the invitation or communication; (ii) if the invitation or communication is oral and delivered in person, such disclosure shall be both oral and in writing and shall be made clearly and conspicuously and in conjunction with the invitation or communication; and (iii) if the invitation or communication is made by telephone, such disclosure shall be made orally and clearly and conspicuously in conjunction with the telephone invitation or communication and in writing by mail to be received by the prospective purchaser at least 24 hours prior to the event or activity; *provided, however,* with respect to subpart (iii) above, that if the event or activity is a sales presentation to be conducted in the home of the consumer, such written disclosure may be made at any time prior to the sales presentation, but in no event shall such disclosure be made later than the introductory remarks of the salesman; and, *further provided,* with respect to subpart (iii) above that if the invitation or communication is received at a place other than the consumer's residence or place of employment, such written disclosure may be made at any time prior to the consumer's attendance at the sales presentation.

2. Misrepresenting the true nature and purpose of any event or activity, including but not limited to dinner parties or other

gatherings, contests, awards of free or reduced gifts or vacations, and sightseeing tours.

3. Failing to furnish the purchaser with a fully completed copy of the contract at the time of its signing by the purchaser, which is in the same language as that principally used in the oral sales presentation, if any, and which shows the date of the transaction and contains the name and address of the respondent; *provided, however,* that a foreign language copy of the contract need not be furnished if the purchaser is literate in the English language; and, *further provided,* that the contract need not at this time contain the signature of respondents.

4. Failing to set forth as the title of any contract for the purchase of land, in boldface type, the following language: "Contract for Deed for the Purchase of Land."

5. (a) Failing to print clearly and conspicuously in 12-point boldface type on the top half of the first page of all contracts for the sale of land, in addition to that language required by Paragraph 4 above, the following:

"THIS IS A CONTRACT BY WHICH YOU AGREE TO PURCHASE LAND. YOU HAVE 10 DAYS IN WHICH TO DETERMINE WHETHER TO CONTINUE THIS CONTRACT OR CANCEL IT WITH FULL REFUND. SEE THE ATTACHED NOTICE OF CANCELLATION FORM FOR AN EXPLANATION OF THIS RIGHT. USE THIS TIME TO EXAMINE WITH CARE THE PROPERTY REPORT (SOMETIMES CALLED A PUBLIC OFFERING STATEMENT) WHICH MUST BE GIVEN TO YOU AT OR BEFORE THE TIME YOU SIGN THIS CONTRACT.

"THE FUTURE VALUE OF THIS LAND, LIKE ALL UNDEVELOPED REAL ESTATE, IS UNCERTAIN. IT IS UNLIKELY THAT A PURCHASER WILL BE ABLE TO RESELL HIS LAND WITHOUT SUBSTANTIAL COMMUNITY DEVELOPMENT AND POPULATION GROWTH, WHICH MAY NOT OCCUR FOR A NUMBER OF YEARS AFTER YOU HAVE COMPLETED YOUR CONTRACT PAYMENTS, IF AT ALL. IT IS SUGGESTED THAT YOU HAVE BOTH THIS CONTRACT AND THE PROPERTY REPORT REVIEWED BY A LAWYER, REALTOR OR OTHER QUALIFIED PROFESSIONAL.

(b) In addition, there shall appear, in the form and place described in subparagraph (a) such of the following statements as are applicable:

(i) For contracts for the sale of lots to which respondents are not obligated to make a central sewer system available at the time title passes to the purchaser, add the following, including the second and third sentence only where applicable:

A central sewer system will not be available when you have completed your contract payments. Installation of a septic tank would be at your expense. However, the use of a septic tank on your lot is contingent on passing a soil test and approval by governmental authorities.

(ii) For contracts for the sale of lots to which respondents are not obligated to make a central water system available at the time title passes to the purchaser, add the following, including the second sentence only where applicable:

A central water system will not be available when you have completed your contract payments. Installation of a well would be at your expense.

(iii) For contracts for the sale of lots to or on which respondents are not obligated to provide any improvements, add the following in lieu of any of the above:

This completely undeveloped land is being sold "as is." No improvements are planned for this subdivision. Your lot is probably inaccessible by conventional means of transportation, and has no use in the present or in the foreseeable future.

6. Failing to include in any contract for the sale of land a provision whereby the seller agrees not to create during the contract term, without the express written permission of the purchaser, by sale, lease or any other means, any restriction, easement or reservation of any kind which can substantially limit the purchaser's use or enjoyment of his lot after the maturity date of said contract.

7. Including in any contract for the sale of land, or in any document shown or provided to purchasers or prospective purchasers of land, whether or not signed by such purchasers or prospective purchasers, language stating expressly or by implication:

(a) That no express or implied representations have been made in connection with the sale of respondents' land, or that any particular representation has not been made in connection therewith; and

(b) That the purchaser has had an opportunity to examine or understand any property report, offering statement or similar document required by state or federal law to be made available to him; *provided, however,* that such language may be included when authorized by the Interstate Land Sales Full Disclosure Act, presently codified at 15 U.S.C. 1701–20 (1970).

8. Changing a contract in any respect after signature by the purchaser unless such change is made by mutual agreement in writing, and unless it is clearly and conspicuously disclosed to the purchaser that he can refuse to accept such change and in lieu thereof receive a full refund of all moneys paid under the contract.

9. Making any statement or representation concerning the rights or obligations of respondents or the purchaser which differs in any material respect from the rights or obligations of the parties as stated in the contract.

10. (a) Representing that respondents will provide, or that respondents' subdivisions will have available, any recreational facility, improvement (roads or drainage) or utility (central sewage and water systems, electricity, or telephone service), unless respondents' contracts at the time of the representation contain a legal obligation on the part of respondents to provide or make available (i) said recreational facilities and improvements at a date certain, not later than 12 years from the date of purchase, set out clearly and conspicuously in the contract; (ii) said utilities within 90 days after respondents' receipt of written notification of the issuance of a building permit, provided that, if so represented, the time for installation of central water and sewer systems may be stated in the contract in terms of population density rather than as a specific date or time; and (iii) without, in the case of improvements or utilities, any cost to the purchaser in excess of the purchase price stated in the contract, except hook-up or installation charges for utilities as estimated in the contract on a current cost basis, subject to future local adjustments in accordance with regulations of and tariffs filed with appropriate public authorities.

(b) Failing to express the aforesaid contractual obligation set out in subparagraph (a) above in the contract with the purchaser in the following manner:

(i) An adequate description of each improvement, utility or recreational facility to be provided;

(ii) A provision that in the event any of the improvements, utilities or recreational facilities specified in the contract are not available to the lot which is the subject of the contract or are not completed within six months of the time provided in the contract, respondents will immediately, upon the expiration of said six-month period, provide the purchaser by certified mail, return receipt requested, with notice of such unavailability of or failure to complete the aforesaid improvements, utilities or recreational facilities and of the purchaser's right to exercise within 30 days of receipt of said notice his option to receive an exchange or to cancel and receive a full refund as set out in subparagraph (iii) below;

(iii) An option to the purchaser stated substantially as follows:

In the event that any of the improvements, utilities or recreational facilities specified by the seller in this contract are not available to the lot which is the subject of this contract or are not completed within six months of the time provided in this contract, the buyer may elect, at his option, to (1) receive an exchange acceptable to the buyer of the contracted-for homesite property for another of at least equal price, equivalent size, with equivalent zoning classification and same promised improvements and utilities, and located in the same general geographic area of the subdivision, or (2) cancel this contract and receive from the seller a full refund of all moneys paid under the contract. To exercise this option, the buyer must give notice to the seller by registered or certified mail within 30 days after receipt of notice from the seller of such unavailability of or failure to complete the aforesaid improvements, utilities or recreational facilities. Where the buyer has received a deed or other evidence of interest in the contracted-for property other than this contract, the buyer must, as a condition of obtaining an exchange or a refund hereunder, reconvey to the seller such evidence of interest in the title to such property by General Warranty Deed in recordable form. In the event only the contract has been recorded in the Public Records, the buyer must quit claim in recordable form his interest to the seller to remove any clouds on the title to said property.

(c) Failing to make the exchange or refund requested by a purchaser under the terms of this paragraph of the order within 60 days of receipt of notification from the purchaser.

(d) Soliciting or obtaining the purchaser's assent to or otherwise imposing any condition, waiver or limitation upon the right of a purchaser to an exchange or a refund as set forth in this paragraph of the order; *provided, however,* that respondents may require purchasers to request an exchange or a refund within a stated time period of not less than 30 days after receipt by the purchaser of the notice required by subparagraph (b)(ii) above.

11. (a) Failing to furnish each purchaser of land, at the time he signs the contract, with a completed form in duplicate, captioned "NOTICE OF CANCELLATION," which shall contain in boldface type of a minimum size of 10 points the following statement:

NOTICE OF CANCELLATION

(date of transaction)

____

(print Purchasers' names)

YOU MAY CANCEL THIS TRANSACTION, WITHOUT ANY PENALTY OR OBLIGATION, AT ANY TIME PRIOR TO MIDNIGHT OF THE TENTH (10th) DAY AFTER THE ABOVE DATE.

IF YOU CANCEL, ANY PAYMENTS MADE BY YOU UNDER THE CONTRACT WILL BE REFUNDED WITHIN TEN (10) BUSINESS DAYS FOLLOWING RECEIPT BY THE SELLER OF YOUR CANCELLATION NOTICE. TO CANCEL THIS

TRANSACTION, MAIL OR DELIVER A SIGNED COPY OF THIS CANCELLATION NOTICE OR ANY OTHER WRITTEN NOTICE, OR SEND A TELEGRAM, TO *(name of respondent)*, AT *(address of respondent's place of business)* NOT LATER THAN MIDNIGHT OF *(date)*.

I (WE) HEREBY CANCEL THIS TRANSACTION. (EACH PURCHASER MUST SIGN THIS NOTICE).

(Date) ________________

(Purchasers' signatures)

(b) Failing, before furnishing copies of the "Notice of Cancellation" to the purchaser, to complete both copies by entering the name of the respondent, the address of the respondent's place of business, the date of the transaction, and the date, not earlier than the tenth day following the date of the transaction, by which the purchaser may give notice of cancellation.

12. Failing, in any instance where a timely notice of cancellation as required by Paragraph 11 above is received, and said notice is not properly signed, and respondents do not intend to honor the notice, immediately to notify the purchaser by certified mail, return receipt requested, enclosing the notice, informing the purchaser of his error, and stating clearly and conspicuously that a notice signed by each purchaser must be mailed by midnight of the third day following the purchaser's receipt of said mailing if such purchasers are to obtain a refund.

13. Failing or refusing to honor any signed and timely notice of cancellation by a purchaser, including any such notice received in accordance with Paragraph 12 above, and within ten business days after the receipt of such notice, to (i) refund all payments collected under the contract, and/or (ii) cancel and return any negotiable instrument executed by the purchaser and retained by respondents in connection with the contract.

14. Negotiating, transferring, selling or assigning any note or other evidence of indebtedness of a purchaser of land to a finance company or other third party prior to midnight of the fifteenth business day following the day the contract was signed.

15. Whenever the signature of a prospective purchaser of land is solicited during the course of a sales presentation, failing to inform each purchaser orally, prior to or at the time he signs the contract, of his right to cancel as provided for in Paragraph 11 above.

16. Requiring the purchaser to make a personal inspection of his lot, the subdivision in which it is located, or any other property, as a condition precedent to the cancellation of any contract or the refund

of any moneys paid thereunder, unless respondents (a) allow such purchaser two business days following the date of inspection within which to cancel, and (b) provide the purchaser at the time of inspection with a notice which clearly and conspicuously states (i) that the purchaser has two business days within which to cancel, (ii) that, in order to cancel, the purchaser must give respondents written notification by registered or certified mail of his desire to cancel, (iii) the final date by which the purchaser must mail such notice of cancellation, and (iv) the address where such notice must be sent; *provided, however,* that nothing in this paragraph of the order shall permit respondents to condition any other cancellation rights provided for in this order on the purchaser's inspection of any property.

17. Failing to comply with Section 226.9 of Regulation Z, 12 C.F.R. 226.9, or its successor regulation.

18. Failing to disclose, clearly and conspicuously, in all promotional materials and advertisements relating to the sale of land, the following statement: "Since land values are uncertain, you should consult a qualified professional before purchasing." *Provided, however,* that the above statement shall not be required in the following:

(a) billboards;
(b) radio and television advertisements of ten seconds or less;
(c) the following advertisements when limited to soliciting requests for information through the mail:

(i) Magazine advertisements of 1/4 page or less in size;
(ii) Newspaper advertisements of 1/8 page or less in size;
(iii) Radio advertisements of more than ten seconds but not more than 45 seconds in duration.

19. Representing:

(a) That the purchase of a lot in one of respondents' subdivisions is a way to insure financial security or to become wealthy;
(b) That real estate is a good or safe investment, or that the purchase of a lot in one of respondents' subdivisions is a good or safe investment;
(c) That land is becoming scarce; or
(d) That the value of any land, including lots being offered for sale or previously sold by respondents, has increased, or will or may increase, or that purchasers have made, or will or may in the future make, a profit by reason of having purchased respondents' land.

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20. Misrepresenting the past, present or future sales price of lots in respondents' subdivisions.

21. Making any representation in connection with the sale of land which in any manner refers to or concerns, directly or by implication, investment in stocks, insurance, banks, or any other form of investment other than respondents' land.

22. (a) Directly stating that airports, Walt Disney World, tourism or industry may or will increase the price or value of any land or other real property sold or being offered for sale by respondents.

(b) Representing data or statistics concerning the growth or development of any geographic area or the business or industry in any geographic area, unless such representations are true and respondents have at the time of making such representations, and maintain for three years thereafter, adequate substantiation for such representations; *provided, however,* that in the event such substantiation consists of data or statistics compiled by any governmental agency which are readily available to respondents, respondents need not retain such substantiation in their possession.

23. (a) Representing in any written promotional or advertising materials relating to the sale of respondents' land, including written materials prepared for use by respondents' salesmen in oral sales presentations, that the population of any geographic area other than respondents' subdivisions has increased, is increasing, or will increase unless respondents have, at the time of making such representation, and maintain for three years thereafter, a valid study or report which demonstrates that respondents' subdivisions within such geographic area or in the general vicinity thereof will materially benefit from said population increase.

(b) Making any representation concerning the population of any geographic area, including the representations referred to in subparagraph (a) above, unless such is the fact and unless respondents have at the time of making such representation, and maintain for three years thereafter, substantiating data which shall consist of a valid census or other valid report or study; *provided, however,* that in the event such substantiation consists of data or statistics complied by any governmental agency which are readily available to respondents, respondents need not retain such substantiation in their possession.

24. Representing that respondents will buy back lots from or resell lots for purchasers, unless such is the fact.

25. Representing that respondents will provide, or that respondents' subdivisions will have available, any recreational facility, without clearly disclosing in immediate conjunction therewith and

with the same conspicuousness as such representation (a) the year by which such recreational facility will be completed, and (b) the current approximate cost to purchasers and to their families of membership in and use of such facilities; or misrepresenting the recreational facilities available at respondents' subdivision generally or from individual lots therein.

26. Representing that waterfront property provides access by boat to the Atlantic Ocean, Gulf of Mexico, or any other body of water, or that canals are navigable or can be used for any recreational activity, unless such is the fact and unless all significant qualifications pertaining to such access, navigability or use are clearly disclosed in immediate conjunction therewith and with the same conspicuousness as such representation.

27. Representing that Golden Gate:

(a) has shopping facilities or stores without clearly disclosing in immediate conjunction therewith and with the same conspicuousness as such representation the nature or extent of these facilities;

(b) has resort facilities without clearly disclosing in immediate conjuction therewith and with the same conspicuousness as such representation that Golden Gate does not have beaches or fishing and boating facilities, unless the contrary is in fact true.

28. Representing:

(a) That River Ranch Acres or Remuda Ranch Grants will be developed in any manner;

(b) That all purchasers of lots in River Ranch Acres or Remuda Ranch Grants can make substantial use of their lots in the present or in the future; or

(c) That purchasers of land have the right to lease to third persons or otherwise have any rights of enjoyment or possession during the contract term in the lots which they have agreed to purchase, unless such is the fact.

29. Assigning similar names to new subdivisions in which the facilities, improvements, and utilities available in such subdivisions are not substantially identical.

30. (a) Making any representation concerning Cape Coral or any other homesite subdivision at a sales presentation at which one or more lots not located in a homesite subdivision are being offered for sale; or

(b) Making any representation concerning any improvement, utility or recreational facility at one subdivision at a sales presentation for another subdivision at which respondents have not provided and are not obligated to provide similar improvements, utilities, or recreational facilities unless respondents disclose in immediate conjunction therewith and with the same conspicuousness as such representation that similar improvements, utilities, or recreational facilities will not be provided at the subdivision to which the advertisement or sales presentation is directed.

31. Misrepresenting the amount, proportion or magnitude of roads of canals completed or under construction in any subdivision.

32. Misrepresenting the qualities, characteristics, location or state of present or planned development of any subdivision or portion thereof.

33. Making any statement or representation concerning the proximity of any city or place to a subdivision or a part thereof without clearly disclosing in immediate conjunction therewith and with the same conspicuousness as such representation the approximate distance in road miles from the geographic center of the subdivision or part thereof to the other city or place referred to.

34. Making any statement or representation concerning the purchase price of land without clearly disclosing in immediate conjunction therewith and with the same conspicuousness as such statement or representation the nature and estimated amount of any additional payments, including but not limited to payments for property taxes, which must be made by the purchaser to respondents or to any third party in order to purchase such land.

35. Representing that central sewage and/or water systems will be available in a subdivision when a given level of population density is reached unless it is clearly disclosed in immediate conjunction therewith and with the same conspicuousness as such representation that purchasers will be required to install, at their own expense, wells and septic tanks until said level of population density is reached.

36. (a) Representing that free or low cost transportation to or accommodations at respondents' subdivisions will be provided unless such is the fact and without clearly disclosing in immediate conjunction therewith and with the same conspicuousness as such representation all conditions or limitations applicable thereto.

(b) Failing to provide the aforesaid transportation or accomodations on the date or within the time period stated or agreed upon; *provided, however,* that it shall not be a violation of this paragraph of the order if such transportation or accommodations are not available due to conditions beyond the control of respondents.

(c) In the event the aforesaid transportation or accomodations are not provided on the date or within the time period stated or agreed upon, failing within 30 days to offer to refund and, upon request by the purchaser, to refund all moneys paid (i) under a contract entered into prior to said failure to provide such transportation or accommodations, and (ii) toward such transportation or accommodations; *provided, however,* that respondents shall not be required to make refunds under subpart (i) above if such transportation or accommodations are not available due to conditions beyond the control of respondents.

37. Making any statement concerning any credit, refund or other monetary benefit or remuneration to purchasers or prospective purchasers unless such is the fact and without clearly disclosing in immediate conjunction therewith and with the same conspicuousness as such statement all conditions and limitations applicable to such credit, refund, benefit, or remuneration.

38. Referring to any instrument or document as a "credit check" or otherwise representing that a credit toward a purchaser's account is an actual payment to the purchaser in the form of cash, check, or other negotiable instrument.

39. Representing that persons being solicited to purchase respondents' land are being asked to take the first step, or are reserving the land, or are not making a final decision, or are not buying the land; or otherwise misrepresenting the legal significance of signing a contract.

40. Representing that prospective purchasers must sign a contract immediately in order to assure purchasing property in a choice location, or that property similar to that being offered for sale may not or will not be available or available at the same price in the foreseeable future, unless such is the fact.

41. In connection with the sale of land:

(a) Representing that increasing the amount of the monthly payment will speed up passage of title, unless such is the fact;

(b) Representing that increasing the amount of the monthly payment will speed up completion of improvements; or

(c) Misrepresenting the benefits to be obtained by increasing the amount of the monthly payment or by completing payment of the purchase price prior to the date the final payment is due under the contract.

42. Representing that any document, sales presentation, advertisement or promotional material has been filed with or approved by any State, the Federal Department of Housing and Urban Develop-

ment, the Armed Forces, or any other governmental agency, unless such is the fact; or representing that governmental regulation means that respondents' representations are true, complete, or should be relied upon; or representing that respondents are affiliated in any manner with the Armed Forces of the United States or any government or governmental agency.

43. Including in any contract or other document any waiver, limitation or condition on the right of a purchaser to cancel a transaction or receive a refund under any provision of this order, except as such waiver, limitation or condition is by this order expressly allowed; *provided, however,* that this paragraph shall not be construed as prohibiting respondents from conditioning the purchaser's right to cancel and receive a refund under any provision of this order on the purchaser's relinquishing and, where appropriate, reconveying to respondents his interest in the land which is the subject of the transaction being cancelled.

44. Misrepresenting the right of a purchaser to cancel a transaction or receive a refund under any provision of this order or any applicable statute or regulation.

45. Making any representation or taking any action which is inconsistent with or detracts from the effectiveness of this order.

It is further ordered, That respondents, upon receipt of a complaint from a purchaser alleging facts that indicate this order may have been violated and requesting a refund or cancellation of the purchaser's contract, refund all moneys paid by such purchaser where respondents determine, after a good faith investigation, that one or more of the paragraphs in Section I of this order have been violated in connection with such purchaser's transactions with respondents; *provided, however,* that in the event respondents refund any money pursuant to this paragraph of the order, the sole fact of such refund shall not be admissible against respondents in any proceeding brought to recover penalties for alleged violation of any other paragraph of this order; and, *further provided,* that this paragraph shall not be applicable to transactions in which the contract was entered into prior to the date this order became final.

II.

It is further ordered, in connection with the refund of moneys forfeited under contracts in default prior to the date this order becomes final:

A. That respondent compile a list of the last known name and address of all persons entering into contracts for the purchase of respondent's land who defaulted on said contracts and forfeited monies paid in excess of the sum of the downpayment plus an amount equal to 30 standard monthly payments as stated in the contract, said list to contain all such forfeitures from July 1, 1968 to October 11, 1974; *provided, however,* that for contracts which were entered into or amended as a result of an exchange by which land purchased pursuant to a single contract was exchanged for land with a higher total price, the terms of the original contract entered into by the purchaser prior to such exchange shall be used to compute the sum of the downpayment and an amount equal to 30 standard monthly payments.

B. That the refund payments due to purchasers pursuant to this section shall be scheduled by the Co-Trustees and shall be provided for in a confirmed plan of reorganization as general unsecured claims entitled to payment at no less a rate or preference than any other general unsecured claims, including claims of bond and debenture holders. All such purchasers shall be notified of the disposition of their claims in conjunction with the notices and plan materials required to be mailed to creditors under Bankruptcy Rule 10-303(e). Upon the return of any notices undelivered, the purchasers affected shall receive notice as directed by the Bankruptcy Court pursuant to Bankruptcy Rule 10-405, fixing a time not less than five (5) years after the final decree closing the estate within which such purchasers may claim the distribution provided for them under the Plan. Upon the expiration of such period, any distribution unclaimed by such purchasers shall revert to the reorganized company, but the fair market value as of such date shall be added to the accrual Reserve Fund provided for under Section III of the Commission Order of 1974, as herein modified.

C. Respondent shall maintain, for a period of five (5) years after the date of the confirmation of the plan of reorganization all records which disclose respondent's compliance with this section of the order, as modified.

III.

It is further ordered, in connection with lot purchasers or titleholders holding contracts for or title to parcels of land in Golden Gate Estates (for purpose of this section, "titleholders" shall not include persons who acquired such title from Collier County, Florida by tax deed):

A. That respondent shall make available to each lot purchaser or titleholder of parcels of land in Golden Gate Estates which are *South* of Stewart Boulevard the choice of one of the following alternatives:

1. Each lot purchaser or title holder may choose to deed his

property to respondent upon the Co-Trustees' scheduling his or her claim for all principal and interest paid to respondent and the provision for such claims as unsecured claims in a confirmed plan of reorganization. Claims hereunder shall be allowed in full, or in *pro rata* amounts totalling not more than $18,000,000 which is the maximum amount of claims that will be allowed under this paragraph. Claims under this paragraph shall be treated as follows:

a. Payments made by lot purchasers or titleholders subsequent to December 12, 1975 shall be granted priority status and, in the event of a successful reorganization plan, shall be paid in cash;

b. The remainder of claims under this paragraph shall be allowed *pro rata* after deducting the claims paid under subparagraph (a) of this paragraph from the allowable maximum of $18,000,000 as general unsecured claims entitled to payment at no less a rate or preference than any other general unsecured claims including claims of bond and debenture holders.

2. Each lot purchaser or titleholder may choose an exchange into River Ranch Acres, on a two-for-one basis, so that each lot purchaser or titleholder will receive double the acreage in River Ranch Acres as is presently owned in Golden Gate Estates. The selection of this alternative shall be limited to the inventory of land in River Ranch Acres owned by respondent as of May 1, 1978, depleted only by the acreage used by respondent to comply with Section IV of this order. In the event a lot purchaser or titleholder who has elected this alternative is unable to receive the double acreage in River Ranch Acres as provided by this paragraph, respondent shall notify each such lot purchaser or titleholder in writing within thirty (30) days after such fact becomes known to respondent that the lot purchaser or titleholder must select one of the remaining alternatives in this section.

Each lot purchaser or titleholder who chooses this option shall remain obligated for any sums remaining due on an existing contract.

3. Each single parcel lot purchaser or titleholder, such lot comprising approximately 1-1/4 acres, may choose an exchange for a developed homesite lot (which for purposes of this order shall be deemed to include improvements consisting of paved streets and drainage, with central water and sewage service to the property line of such homesite; standard electrical service shall be available, at nominal charge, to each homesite within 180 days of the issuance of a building permit) in the Poinciana subdivision with the lot purchaser or titleholder to pay development costs of $2,300. The development costs to be paid by the lot purchaser or titleholder shall

be in addition to any sums due under any existing contract with respondent. The development costs may be paid, at the option of the lot purchaser or titleholder, either in a lump sum or in deferred payments over not more than seven (7) years at the rate of 7.5% interest per annum. Although development costs may be payable over a seven (7) year period, the homesites shall be developed by respondent over a three (3) year period commencing immediately upon confirmation of a plan of reorganization. If the development costs are paid in a lump sum, respondent shall immediately issue a deed to the homesite and cause to be issued a policy of title insurance, subject only to the respondent's inventory of completed homesites in the Poinciana subdivision at the time the development costs are paid in a lump sum.

4. Each multi-parcel lot purchaser or titleholder may choose an exchange for each 2 1/2 acre lot in Golden Gate Estates to one developed homesite lot in the Poinciana subdivision at no additional cost to the lot purchaser or titleholder except for a charge of $1,150 for water and sewer betterment fees. The water and sewer betterment fees shall be in addition to any sums due under any existing contract with respondent. The betterment fees may be paid, at the option of the lot purchaser or titleholder, either in a lump sum or in deferred payments over not more than seven (7) years at the rate of 7.5% interest per annum. Although such betterment fees may be payable over a seven (7) year period, the homesite shall be developed over a three (3) year period commencing immediately upon confirmation of a plan of reorganization. If such betterment fees are paid in a lump sum, respondent shall immediately issue a deed to the homesite and cause to be issued a policy of title insurance, subject only to the respondent's inventory of completed homesites in the Poinciana subdivision at the time the betterment fees are paid in a lump sum. After selecting this option of one developed homesite lot in the Poinciana subdivision, each multi-parcel lot purchaser or titleholder may choose other alternatives in this section in exchange for any remaining lands in excess of the 2 1/2 acre lot exchanged pursuant to this paragraph.

5. Each lot purchaser or titleholder may choose an exchange toward the land portion only of a "Housing Construction Package" at any on-going development project of the respondent, each lot purchaser or titleholder being entitled to full credit for all paid-in principal and interest, limited, however, to payments made to respondent on not more than one 2 1/2 acre parcel of Golden Gate Estates per exchanging lot purchaser or titleholder. If a lot purchaser or titleholder has two or more Golden Gate Estates parcels, he or

she may choose two or more "Housing Construction Packages" or one or more packages for each 2 1/2 acres and choose other alternatives in this section in exchange for the remaining land. Lot purchasers or titleholders choosing this option shall have five (5) years from the date of confirmation of a plan of reorganization within which to contract for a housing construction package at the terms (including price) and conditions being offered by the respondent at the time such contract is executed.

B. For all lot purchasers or titleholders of parcels of land in Golden Gate Estates *North* of Stewart Boulevard, respondent shall on the date of confirmation of a plan of reorganization estabish an accrual Reserve Fund in the amount of $10,000,000. This Reserve Fund shall be maintained by respondent for a period of five (5) years following confirmation of a plan of reorganization or until the Reserve Fund has been depleted or exhausted, whichever event occurs first. After the fifth year, the funds under Section II which revert to the accrual Reserve Fund shall be immediately available for use under this section to pay any claim filed prior to the expiration of the five (5) year period. All claims payable under this section shall be paid in full on a first come, first served basis.

1. At any time after the date of confirmation of a plan of reorganization of the respondent, and no later than five (5) years after such date, each lot purchaser or titleholder of parcels of land in Golden Gate Estates *North* of Stewart Boulevard may, at his own expense, have a test or tests made to determine the percolation of his lot and/or the availability of an adequate supply of potable water. The lot purchaser or titleholder shall then provide respondent with such test report or reports, prepared by a Registered Professional Engineer or Registered Analytical Laboratory, certifying the failure of the lot to pass a percolation test or the inability to obtain potable water. For purposes of this order, "potable water" shall be defined as drinkable water that poses no threat to health by exceeding the maximum contaminant levels set by regulations of the U.S. Environmental Protection Agency under the Safe Water Drinking Act, as provided in 40 C.F.R. Part 141 as of the date of this order modifying the Commission Order of 1974, for inorganic and organic chemicals and coliform bacteria, and complies with all other applicable Federal, state and local standards for individual water supply systems.

2. With respect to any lot or parcel of land requiring expenditures for remedial work for percolation of less than $2,500, the first $1,000 of the expenditures for remedial work, which amount shall include the cost of having the test or tests made, shall be the

responsibility of the lot purchaser or titleholder. Each lot purchaser or titleholder shall present to respondent a test report or reports certified by a Registered Professional Engineer that the remedial work will exceed $1,000 but not be more than $2,500. Within thirty (30) days after receipt of the certified report or reports from the lot purchaser or titleholder, respondent shall at its option:

a. Pay the excess of $1,000 to the lot purchaser or titleholder and charge such payment to the Reserve Fund; or

b. Request that the lot purchaser or titleholder pay to respondent the actual cost of doing the work, but not more than $1,000, less the cost of the test or tests paid by the lot purchaser or titleholder, and subsequently do the remedial work itself within sixty (60) days and charge the Reserve Fund with the difference, if any, between $1,000 and the actual cost of doing the work. Such charge to the Reserve Fund shall not exceed $1,500.

3. With respect to any lot or parcel of land requiring expenditures for remedial work for percolation in excess of $2,500, each lot purchaser or titleholder shall present to respondent a test report or reports certified by a Registered Professional Engineer that the remedial work will exceed $2,500. Within thirty (30) days after receipt of the certified report or reports from the lot purchaser or titleholder, respondent shall:

a. Exchange the lot purchaser or titleholder into a Golden Gate Estates land parcel *North* of Stewart Boulevard of equal size as the lot purchaser's or titleholder's existing parcel and provide the lot purchaser or titleholder with a Registered Professional Engineer's certificate certifying the percolation of such lot in its existing state without remedial work and the availability of an adequate supply of potable water in a well existing on such parcel as of the date of exchange; or

b. If respondent has no lots with adequate percolation and with an adequate supply of potable water available to offer under subparagraph (a) of this paragraph, respondent may do remedial work for a cost of not more than $3,000 per lot (including well-drilling) on available inventory of land *North* of Stewart Boulevard in order to certify both percolation and the availability of an adequate supply of potable water in an existing well on such parcel. Thereafter, respondent may charge a lot purchaser or titleholder exchanged into such lot the actual cost of the remedial percolation work or $1,000, whichever is less (minus the amount paid by such lot purchaser or titleholder for remedial percolation work on the parcel to be exchanged by such lot purchaser or titleholder) and the actual cost of well-drilling or $500, whichever is less (unless the lot purchaser or titleholder has previously had a well drilled on his former lot, in which case no charge shall be made for well-drilling). Respondent may thereafter charge one-half (1/2) the cost of remedial work and the full cost of well-drilling up to $500, less the amount received from the lot purchaser or titleholder, to the Reserve Fund; or

c. If no parcels in respondent's inventory remain which qualify for exchange under subparagraphs (a) or (b) above, refund to the lot purchaser or titleholder, in cash, from the Reserve Fund all principal paid in to respondent. In conjunction with the offer of such refund, or if no funds are available for such refund, respondent shall also offer the lot purchaser or titleholder, in lieu thereof, the choices provided in subparagraphs (A) (3)–(5) of this section.

In the event of a lot exchange or cash refund pursuant to this paragraph, the lot purchaser or titleholder shall be required to deed his or her property to respondent.

4. With respect to any lot purchaser or titleholder who provides respondent with certification of the inability to obtain an adequate supply of potable water, respondent shall:

a. Perform such remedial work as is necessary to obtain an adequate supply of potable water, including the deepening or shallowing of the existing well or the drilling of an additional well on the same site. The cost of such work shall be borne by the respondent, but no more than $500 of the cost of such work may be charged to the Reserve Fund;

b. If the remedial work under subparagraph (a) of this paragraph cannot be performed for less than $500 or if an adequate supply of potable water is not produced thereby, exchange the lot purchaser or titleholder into a Golden Gate Estates land parcel *North* of Stewart Boulevard of equal size as that of the lot purchaser or titleholder and provide a certificate of a Registered Professional Engineer that the parcel passes a percolation test in its existing state without remedial work and that an adequate supply of potable water is available in a well existing on such parcel as of the date of the exchange. If the lot purchaser or titleholder has not had a well drilled, respondent may, as part of the exchange, require a payment of not more than $500 from the lot purchaser or titleholder to cover the actual cost of drilling the well.

c. If respondent has no lots with adequate percolation and with an adequate supply of potable water available to offer under subparagraph (b) of this paragraph, it may do remedial work for a total cost of not more than $3,000 per lot (including well-drilling) on available inventory *North* of Stewart Boulevard in order to certify both the percolation and availability of an adequate supply of potable water in a well existing on such parcel as of the date of exchange. Thereafter, respondent may charge a lot purchaser or titleholder exchanged into such parcel the cost of the remedial percolation work or $1,000, whichever is less (minus the amount paid by such lot purchaser or titleholder for remedial percolation work on the parcel to be exchanged by such lot purchaser or titleholder). Respondent may thereafter charge the Reserve Fund for one-half (1/2) the actual cost of the remedial work and the full cost of well-drilling up to $500, less the payment received from the lot purchaser; or

d. In the event that the remedial work or exchanges required by subparagraphs (a) - (c) of this paragraph cannot be performed as specified therein, refund to the lot purchaser or titleholder, in cash, from the Reserve Fund, all principal paid in to respondent. In conjunction with the offer of such refund, or if no funds are available for such refund, respondent shall also offer the lot purchaser or titleholder, in lieu thereof, the choices provided in subparagraphs (A)(3)-(5) of this section.

C. The appropriate letter, as set forth in Appendices (1) or (2) of this order modifying the Commission Order of 1974, shall be sent by respondent to all persons holding contracts for or title to land in Golden Gate Estates along with the claims bar order to be entered by the Bankruptcy Court fixing the claims deadline for claims relating to Golden Gate Estates. Respondent shall take all reasonable measures to obtain the current mailing address of such persons, including obtaining current addresses from the tax rolls of Collier County, Florida for the Golden Gate Estates subdivision.

D. Respondent shall, on the date the Commission accepts the order provisionally modifying the Commission Order of 1974, immediately establish an accrual fund in the amount of $200,000 to be used, as directed by the Federal Trade Commission or its representative, to notify by any means, including advertising by newspaper, magazine or television, persons holding contracts for or title to land in Golden Gate Estates of the options provided in this section, and persons entitled to refunds under Section II of the Commission Order of 1974, as modified. No charges for mailing letters under paragraph (C) of this section shall be charged to this fund. The amount required to be available under this paragraph shall remain available until five (5) years after the date of confirmation of a plan of reorganization or until exhausted, or until released by the Commission, whichever first occurs. Any funds charged to the fund established by this paragraph shall be subsequently charged to the accrual Reserve

Fund established pursuant to paragraph (B) of this Section. If the accrual Reserve Fund is exhausted before the fund established in this paragraph is exhausted, no further funds will be available under this paragraph.

E. Respondent shall maintain, for a period of seven (7) years after the date of confirmation of a plan of reorganization, all records which disclose respondent's compliance with this section of the order, as modified.

IV.

For purposes of this section of the order, the following definitions shall be applicable:

When used in reference to land at Remuda Ranch Grants or River Ranch Acres, "lot" shall mean a parcel of land approximately 1-1/4 acres in size, and "lots" shall mean a parcel or parcels of land purchased pursuant to a single contract with respondent GAC Properties Inc. or its predecessor Gulf American Corporation, the total acreage of which is a multiple of the approximately 1-1/4 acre parcel comprising a lot.

It is further ordered, in connection with the exchange of land purchased in Remuda Ranch Grants and River Ranch Acres:

A. That respondents compile a list containing the last known name and address of the purchaser and date of purchase for each contract for the purchase of a lot or lots in Remuda Ranch Grants or River Ranch Acres where the purchaser is either deeded or has an outstanding contract not in default, said list to be arranged in chronological order by subdivision and grouped according to the number of lots purchased.

B. That respondents send a letter as set out in Appendix A or B, as applicable, within six (6) months of the date this order becomes final and thereafter in accordance with Paragraph G below, by certified mail, return receipt requested, to the following of the purchasers referred to in Paragraph A above: (1) all purchasers whose date of purchase is January 1, 1969 or later; (2) all purchasers of 3 or more lots whose date of purchase is prior to January 1, 1969; and (3) as many purchasers of 1 or 2 lots whose date of purchase is prior to January 1, 1969 as the inventory of lots set aside for this exchange offer will permit, in accordance with the schedule set out in subparagraph E(6) below.

C. That respondents enclose together with the letter referred to in Paragraph B above the following material:

1. A notice of acceptance form as set out in Appendix C;
2. A document listing (a) the contract number and date of

purchase for the lot or lots in which the purchaser's interest will be relinquished if the exchange offer is accepted, and (b) the legal and/or other adequate description and approximate size concerning both the lot or lots being offered in exchange and the lot or lots in which the purchaser's interest will be relinquished if the exchange offer is accepted;

3. The applicable property report for the lot or lots being offered in exchange; and

4. A map or maps showing the location in the subdivision and, where available, the block or unit of the lot or lots being offered in exchange.

D. That with respect to any letter referred to in Paragraph B above which is returned to respondents undelivered, respondents, within 60 days of receipt of such undelivered letter, shall take measures which are reasonably calculated to obtain the current address of the purchaser and shall deliver said letter to him; *provided, however,* that in the event respondents are unable to deliver such letter within said 60-day period, said offer of exchange shall be deemed rejected by the purchaser for purposes of this order.

E. That respondents, upon receipt of a notice of acceptance of the exchange offer provided for in this section of the Order, shall exchange the lot or lots purchased in Remuda Ranch Grants and/or River Ranch Acres for land in certain of respondents' other subdivisions according to the following schedule:

1. Remuda Ranch Grants - date of purchase January 1, 1969 or later:

(a) A purchaser of 3 or more lots may exchange such lots for lots in Cape Coral which had, or would have had if offered for sale, a selling price on July 1, 1973 equal to or greater than the purchase price of his lots as stated in the contract of purchase; *provided, however,* that no such purchaser shall be offered less than 2 adjacent Cape Coral lots (1 homesite) in exchange for the lots he has purchased.

(b) A purchaser of 1 or 2 lots may exchange such lots for 1 homesite lot in Golden Gate Estates.

2. River Ranch Acres - date of purchase January 1, 1969 or later:

(a) A purchaser of 3 or more lots may exchange such lots for lots in Cape Coral which had, or would have had if offered for sale, a selling price on July 1, 1973 equal to or greater than the purchase price of his lots as stated in the contract of purchase; *provided, however,* that no such purchaser shall be offered less than 2 adjacent Cape Coral lots (1 homesite) in exchange for the lots he has purchased.

(b) A purchaser of 1 or 2 lots may exchange such lot or lots for 1 homesite lot in River Ranch Shores.

3. Date of purchase prior to January 1, 1969:

(a) Remuda Ranch Grants - A purchaser of 3 or more lots may exchange such lots for lots in Golden Gate Estates which had, or would have had if offered for sale, a selling price on July 1, 1973 equal to or greater than the purchase price of his lots as stated in the contract of purchase; *provided, however,* that no such purchaser shall be offered less than 1 Golden Gate Estates lot in exchange for all the lots he has purchased.

(b) River Ranch Acres - A purchaser of 3 or more lots may exchange such lots for lots in Cape Coral which had, or would have had if offered for sale, a selling price on July 1, 1973 equal to or greater than the purchase price of his lots as stated in the contract of purchase; *provided, however,* that no such purchaser shall be offered less than 2 adjacent Cape Coral lots (1 homesite) in exchange for the lots he has purchased.

(c) Remuda Ranch Grants and River Ranch Acres - A purchaser of 1 or 2 lots may exchange lot or lots for 1 lot to be located in either Golden Gate Estates or River Ranch Shores at the discretion of respondents, subject to the inventory of lots set aside for the exchange offer as provided for in subparagraph 4 below.

4. For purposes of the exchange offer provided for in that section, respondents shall make available 3,429 lots in Golden Gate Estates, 7,058 lots in River Ranch Shores, and enough lots in Cape Coral to meet the demands of subparts 1(a), 2(a), and 3(b) above; *provided, however,* that in the event respondents' inventory of lots in Cape Coral should prove insufficient to meet the demands of the exchange offer provided for in this section, lots in Poinciana shall be substituted; and, *further provided,* that in the event any governmental regulation prevents the use of any portion of Golden Gate Estates as provided for in this section of the order, respondents may offer to the applicable purchasers an alternative exchange, acceptable to the Commission, of a homesite lot in another subdivision.

5. (a) The lots in Golden Gate Estates to be offered in exchange pursuant to this section of the order shall be developed in accordance with Section III above.

(b) The lots in Cape Coral, River Ranch Shores, and Poinciana to be offered in exchange pursuant to this section of the order shall be developed in accordance with the most recent applicable property report on file on the date this order becomes final with the Office of Interstate Land Sales Registration of the U.S. Department of Housing and Urban Development; *provided, however,* that in the event no property report is on file with the Office of Interstate Land Sales Registration with respect to any lot in Cape Coral, River Ranch

Shores, or Poinciana which is being offered in exchange pursuant to this section of the order, such lot shall be developed in accordance with the most recent applicable property report or offering statement on file with the State of Florida.

6. For purposes of the exchange offer set out in subpart 3(c) above, such exchanges shall be made until the inventory of lots in Golden Gate Estates and River Ranch Shores set out in subparagraph 4 above is exhausted, subject to the following conditions:

(a) the exchanges shall be offered to all purchasers of 2 lots prior to being offered to purchasers of 1 lot; and

(b) the exchanges shall be offered to purchasers by date of purchase in reverse chronological order (most recent purchase exchanged first).

F. That in the event a purchaser fails to mail a notice of acceptance to respondents within 60 days of his receipt of the letter referred to in Paragraph B above, then for purposes of this order such purchaser shall be deemed to have rejected the exchange offer.

G. That within 120 days of the initial exchange offer set out in Paragraph B above, respondents shall offer all lots referred to in subparagraph E(4) above for which an exchange offer has been rejected to the next purchasers eligible to receive said exchange offer in accordance with subparagraph E(6) above; and respondents shall thereafter continue, at intervals not to exceed 120 days, to offer all lots for which an exchange offer has been rejected to the next eligible purchasers until either all the aforesaid lots have been exchanged or the list of purchasers eligible to receive the exchange offer has been exhausted.

H. That the ten-day right of cancellation provided for in Paragraphs 6 through 10 of Section I of this order shall not be applicable to lots exchanged pursuant to this section of the order.

I. That respondents may condition the exchange offer under this section of the order on the purchaser's execution of a quit-claim deed and/or other documents necessary to release his interest in the lot or lots being given up in exchange, such document or documents to be prepared by respondents.

J. That respondents maintain, for three years after the final exchange is made pursuant to this section of the order, records which are adequate to disclose respondents' compliance with this section of the order, such records to be furnished by respondents to the Federal Trade Commission upon request.

K. That it shall be deemed full compliance with the provisions of this section if respondent (1) sends a letter, as set forth in Appendices (3) or (4), as appropriate, to the order modifying the

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Commission Order of 1974, within ninety (90) days after a plan of reorganization has been confirmed by the Bankruptcy Court, by certified mail, return receipt requested, to the lotholders or titleholders who remain entitled to an exchange under Section IV of the Commission Order of 1974, such mailing to continue until 924 Remuda Ranch Grants lot purchasers or titleholders and 3,858 River Ranch Acres lot purchasers or titleholders acknowledge receipt thereof; and (2) provides the lot purchaser or titleholder with the option selected. Each such lot purchaser or titleholder shall be offered the choice of the following options:

(1) For those in River Ranch Acres, additional unimproved land in River Ranch Acres equal to their present acreage in size; for those in Remuda Ranch Grants, an exchange into River Ranch Acres, on a two-for-one basis, so that each lot purchaser or titleholder will receive double the acreage in River Ranch Acres as is presently owned in Remuda Ranch Grants; subject only to the availability of respondent's inventory of such land as of May 1, 1978. For those already holding title to or contracts for land in River Ranch Acres, the additional acreage offered hereunder shall be contiguous to the extent possible. Offers of land under this section shall take priority over exchanges offered under Section III of the Commission Order of 1974, as modified.

(2) An exchange to a homesite lot in the Poinciana subdivision under the conditions as set forth in Section III (A)(3)–(4) of the Commission Order of 1974, as modified.

(3) An exchange to a Housing Construction Package at any ongoing GAC development project under the conditions as set forth in Section III (A)(5) of the Commission Order of 1974, as modified.

In the event any lot purchaser or titleholder who acknowledges receipt of a letter mailed pursuant to this section has not responded within sixty (60) days, such recipient shall be deemed to have rejected the alternatives provided by this section.

L. Respondent shall maintain, for a period of five (5) years after the date of confirmation of the plan of reorganization, all records which disclose respondent's compliance with this section of the order, as modified.

V.

For purposes of this section of the order, the following definition shall be applicable:

"Residential property" shall mean land located in a subdivision in which the majority of lots are sold or offered for sale for use as homesites.

It is further ordered:

A. (1) That respondents shall include the following language, or words of similar import and meaning, in all installment contracts for the sale of residential property to consumers which are entered into after the date this order becomes final, and shall make refunds in accordance therewith:

In the event of Buyer's default, Seller shall refund to Buyer within 180 days of the date of default principal payments (not interest, finance charges or taxes) made pursuant to this contract in accordance with the following schedule of refunds:

a. If Buyer's total principal payments do not exceed 30% of the cash price, Buyer shall not receive any refund whatsoever.

b. If Buyer's total principal payments exceed 30% but are less than 66-2/3% of the cash price, Buyer shall receive a refund of two-thirds of all principal payments made in excess of 30% of the cash price.

c. If Buyer's total principal payments are in excess of 66-2/3% of the cash price, Buyer shall receive a refund of one-half of all principal payments made in excess of 66-2/3% of the cash price, together with and in addition to all sums refundable to Buyer under subpart b above.

(2) That in the event the rate of default for all contracts for the sale of respondents' land to consumers in which the amount of principal paid exceeds 30% of the cash price due thereunder, which are entered into during the ten-year period after the date this order becomes final, does not exceed by more than ten percent the rate of default, computed in the same manner, for all such contracts for the three-year period immediately preceding the date this order becomes final, the following schedule of refunds shall be included by respondents in all installment contracts for the sale of residential property to consumers which are entered into more than 90 days after the expiration of said ten-year period, in lieu of the schedule of refunds set out in subparagraph A(1) above:

a. If Buyer's total principal payments do not exceed 30% of the cash price, Buyer shall not receive any refund whatsoever.

b. If Buyer's total principal payments exceed 30% of the cash price, Buyer shall receive a refund of 75% of all principal payments made in excess of 30% of the cash price.

(3) That respondents submit to the Federal Trade Commission, within 90 days after the date this order becomes final, data disclosing

the rate of default referred to in subparagraph A(2) above for the three-year period immediately preceding the date this order becomes final, and documentation in support thereof.

B. That respondents shall include the following language, or words of similar import and meaning, in all installment contracts for the sale of land other than residential property to consumers which are entered into after the date this order becomes final, and shall make refunds in accordance therewith:

In the event of Buyer's default, Seller shall refund to Buyer within 180 days of the date of default principal payments (not interest, finance charges or taxes) made pursuant to this contract in accordance with the following schedule of refunds:

1. If Buyer's total principal payments do not exceed 30% of the cash price, Buyer shall not receive any refund whatsoever.

2. If Buyer's total principal payments exceed 30% of the cash price, Buyer shall receive a refund of 75% of all principal payments made in excess of 30% of the cash price.

C. That respondents may condition their payment of refunds under this section of the order on the purchaser's execution of a quit-claim deed and/or other documents necessary to release his interest in the land purchased from respondents pursuant to the contract in default, such document or documents to be prepared by respondents.

D. That in the event the Federal Trade Commission promulgates a valid Trade Regulation Rule applicable to respondents' sale of land to consumers which regulates the amount or percentage of moneys paid by a purchaser which may be retained by the seller in the event of the purchaser's default, then this section of the order shall be deemed modified by said Trade Regulation Rule; *provided, however,* that this paragraph shall not be construed as waiving or in any way limiting respondents' legal rights or standing to challenge or otherwise contest such a Trade Regulation Rule.

VI.

It is further ordered:

(a) That in the event respondents fail to correct any default under a contract entered into prior to the effective date of this order within six months after receiving notice in writing from the purchaser of said default, respondents shall, within ten days after completion of said six-month period, notify the purchaser that, at his option, he may receive a refund of all moneys paid under the contract or an exchange acceptable to him of the contracted-for property for another of at least equal price, equivalent size, with equivalent zoning classification and same promised improvements and utilities, and located in the same general geographic area of the subdivision. *Provided, however,* that respondent shall not be considered in default of any contract hereunder if all contractual obligations covered by this section are assumed by the company in a plan of reorganization confirmed by the Bankruptcy Court and such obligations are performed within the dates provided in the confirmed plan of reorganization but no later than 1985.

(b) That respondents shall make the exchange or refund requested by the purchaser under the terms of Paragraph (a) above within 60 days of receipt of the purchaser's acceptance of said exchange or refund; *provided, however,* that in the event the purchaser has received a deed or other evidence of interest in the contracted-for property other than the contract, the purchaser must, as a condition of obtaining such refund or exchange, reconvey to the seller such evidence of interest by General Warranty Deed in recordable form; and, *further provided,* that in the event only the contract has been recorded in the Public Records, the purchaser must quit-claim in recordable form his interest to the seller to remove any clouds on the title to such property.

VII.

It is further ordered:

(a) That respondents herein deliver, by hand or by certified mail, a copy of Sections I and VI through X of this order to each of their present or future salesmen, independent brokers, and employees who sell or promote the sale of land or other real property to consumers, and all others so engaged;

(b) That respondents provide each person so described in Paragraph (a) above with a form, returnable to respondents, clearly stating his intention to be bound by and to conform his sales practices to the requirements of this order;

(c) That respondents inform each person described in Paragraph (a) above that respondents shall not use any such party, or the services of any such party, unless such party agrees to and does file notice with respondents that it will be bound by the provisions contained in this order;

(d) That in the event such party will not agree to so file notice with respondents and to be bound by the provisions of this order, respondents shall not use such party, or the services of such party;

(e) That respondents so inform the persons described in Paragraph (a) above that respondents are obligated by this order to discontinue dealing with those persons who engage on their own in the acts or practices prohibited by this order;

(f) That respondents institute a program of continuing surveillance adequate to reveal whether the sales practices of each of said persons described in Paragraph (a) above conform to the requirements of this order; and

(g) That respondents discontinue dealing with any person described in Paragraph (a) above, revealed by the aforesaid program of surveillance, who engages on his own in the acts or practices prohibited by this order; *provided, however,* that violation of any provision of this order by present or future employees of independent brokers shall not be deemed a violation of this order by respondents unless respondents, upon knowledge of such violation, fail to take, within a reasonable time, corrective action to insure that such act or practice is terminated; and *further provided,* that in the event remedial action is taken, the sole fact of such dismissal or termination shall not be admissible against respondents in any proceeding brought to recover penalties for alleged violation of any other paragraph of this order.

VIII.

It is further ordered:

(a) That in the event the Interstate Land Sales Full Disclosure Act, presently codified at 15 U.S.C. 1701–20 (1970), or any regulation promulgated pursuant thereto by the Office of Interstate Land Sales Registration of the U.S. Department of Housing and Urban Development, requires an act or practice which is prohibited by any provision of this order, such order prohibition shall be inoperative.

(b) That in the event any provision of this order requires an act or practice which is prohibited by the Interstate Land Sales Full Disclosure Act, presently codified at 15 U.S.C. 1701–20 (1970), or any regulation promulgated pursuant thereto by the Office of Interstate Land Sales Registration of the U.S. Department of Housing and Urban Development, such order requirement shall be inoperative.

IX.

It is further ordered, That this order shall become effective in accordance with standard Commission procedure; *provided, however,* that all written advertising and promotional materials, and form contracts, which must be filed with and accepted for dissemination by state or federal agencies, shall not be subject to the provisions of this order, except for those provisions which prohibit or limit the use of any statement, representation, or misrepresentation, for a period of six months from the date this order becomes final or until said acceptance for dissemination is obtained from all applicable state or federal agencies, whichever occurs first; and, *further provided,* that until said six-month period expires or said acceptance for dissemination is obtained, whichever occurs first, respondents shall file with the Federal Trade Commission monthly reports detailing respondents' progress toward obtaining the aforementioned acceptance for dissemination by the applicable state or federal agencies.

X.

It is further ordered, That respondent corporations shall forthwith distribute a copy of this order to each of their operating divisions engaged in the sale of land or other real property to consumers.

It is further ordered, That respondents herein shall, within six months after the date of confirmation of a plan of reorganization, and annually for five (5) years thereafter, file with the Commission a report in writing setting forth in detail the manner and form in which they have complied with this order.

It is further ordered, That respondents notify the Commission at least 30 days prior to any proposed change in the corporate respondents, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of this order.

APPENDIX 1

FEDERAL TRADE COMMISSION
WASHINGTON, D. C. 20580

BUREAU OF
CONSUMER PROTECTION

Dear Golden Gate Estates Customer:

As you probably know, GAC Properties, Inc. (formerly Gulf American Corporation) is in bankruptcy. In an effort to protect your interests, as much as possible, the Federal Trade Commission has entered into a new agreement with GAC which gives you a chance to select one of five choices. GAC's records indicate your land is located southof Stewart Boulevard in Golden Gate Estates. Stewart Boulevard is five (5) miles south of Alligator Alley (Florida State Road 858) and is one of the main east-west roads in Golden Gate Estates.

In deciding which choice you should make, you should be aware that most of the land south of Stewart Boulevard in Golden Gate Estates is subject to excessive flooding during Florida's "wet season" and brush fires during the "dry season." Furthermore, Golden Gate Estates will not be developed beyond the limited improvements (roads and canals) that have already been made. Note that there is no central water and sewer system. Telephone and electrical hookups may be very expensive.

The new agreement gives you the right to select one of the following choices:

Choice No. 1: You can deed back your property in Golden Gate Estates to GAC and the GAC Trustees will have a claim scheduled for you in the Bankruptcy Court for all of the principal and interest you have paid to GAC on your contract. If you made payments to GAC after December 12, 1975, these payments will be refunded to you in cash. The balance of your payments will be scheduled as unsecured claims to be shared on a pro rata basis with other purchasers of property south of Stewart Boulevard from a maximum amount of $18 million dollars in claims, less the cash payments refunded. The unsecured claims may not be paid in cash but could be paid by the delivery of stock in the reorganized company.

Choice No. 2: You can deed back your property in Golden Gate Estates to GAC and the company will deed to you twice as much land in River Ranch Acres. The parcels deeded to you in River Ranch Acres might not be next to one another. The land in River Ranch Acres will not be developed in any way and in most areas there are no roads. If you are still paying for your property in Golden Gate Estates and you select this choice, you will still have to make the payments due on your existing contract.

There is no sure way of knowing whether land in River Ranch has any significant value now, or will ever have any significant value. There have been no sales of this land in the last few years. The land is not suitable for homesite use in its present condition.

PLEASE NOTE: There is limited land available in River Ranch Acres. If you select this choice and there is no land available, you will be notified and given a chance to select one of the other choices in this letter.

Choice No. 3: You can exchange each 1 1/4 acres of your property in Golden Gate Estates for a fully developed homesite lot in Poinciana. Poinciana is a GAC homesite subdivision in central Florida. A brochure describing Poinciana has been sent to you by GAC. If you select this choice, GAC will select a lot for you, and you must pay development costs of $2,300 which may be paid at one time or paid over a seven (7) year period at 7 1/2% ANNUAL PERCENTAGE RATE GAC advises that payment over seven (7) years will require 84 consecutive monthly payments of $35.38 each, your FINANCE CHARGE will be $671.92 on the $2,300 amount financed, and your total of payments will be $2,971.92. In addition, regardless of whether you pay at one time or over a seven (7) year period, you will be required to pay annual property taxes plus a monthly association maintenance fee which is presently $10 per month. This association maintenance fee is a standard condition of all contracts and deeds in the Poinciana subdivision GAC also pays annual property taxes and association maintenance fees on the property it owns in Poinciana. Of course, you will still have to pay any amount due on your existing contract.

If you pay the development costs of $2,300 all at once, you will immediately be given full title to a developed homesite lot in Poinciana, unless GAC does not have enough developed lots immediately available. GAC has over 1,000 fully developed lots available right now.

If you choose to spread your payments over time, you will not receive a deed until you are finished making all payments.

Before taking this option, you should understand that your ability to resell land in Poinciana, without a house built on the property, is uncertain at this time.

Take this option only if you want homesite property for residential use, not as an investment.

Choice No. 4: You can exchange each 2 1/2 acres of your property in Golden Gate Estates for a fully developed homesite lot in Poinciana which will be selected for you by GAC for an additional payment of $1,150 for water and sewer betterment fees.

This payment will be in addition to any money still due on your existing contract with GAC. You may pay this additional $1,150 at one time or it may be paid over a seven (7) year period at 7 1/2% ANNUAL PERCENTAGE RATE. GAC advises that payment over seven (7) years will require 84 consecutive monthly payments of $17.64 each, your FINANCE CHARGE will be $331.76 on the $1,150 amount financed, and your total of payments will be $1,481.76. In addition, regardless of whether you pay at one time or over a seven (7) year period, you will be required to pay annual property taxes plus a monthly association maintenance fee which is presently $10 per month. This association maintenance fee is a standard condition of all contracts and deeds in the Poinciana subdivision. GAC also pays annual property taxes and association maintenance fees on the property it owns in Poinciana.

If you pay the development costs of $1,150 all at once, you will immediately be given full title to a developed homesite lot in Poinciana, unless GAC does not have enough developed lots immediately available. GAC has over 1,000 fully developed lots available right now.

If you choose to spread your payments over time, you will not receive a deed until you are finished making all payments.

Before taking this option, you should understand that your ability to resell land in Poinciana, without a house built on the property, is uncertain at this time.

Take this option only if you want homesite property for residential use, not as an investment.

Choice No. 5: You can exchange your land for a GAC "Housing Construction Package." All of the principal and interest you have paid to GAC, limited to payments made on no more than 2 1/2 acres, will be credited to the land portion only of your "Housing Construction Package." A brochure describing GAC's present "Housing Construction Package" has been sent to you by GAC. If you select this choice, you have up to five (5) years within which to contract with GAC for a "Housing Construction Package", at the terms (including price) and conditions being offered by GAC at the time such contract is executed.

If you are still making payments on your property, you have two (2) choices if you take this option for a housing package.

--- You can stop making your payments. You will lose your land, but you will have a full credit for all the money you have paid if and when you sign a contract for a housing package. Or ....

--- You can continue to make your payments and hold onto your property. Later, if you wish, you can exchange your property for a housing package with a full credit for all the money you have paid.

If you have already fully paid for your property, you will keep it until you decide whether to exchange for a housing construction package.

This option is offered only for those who, within the next five years, want a home in Florida. As a residential investment, the value of this option is highly speculative.

To accept one of the choices listed as 1 through 5 above, you must sign and return to GAC the enclosed NOTICE OF ACCEPTANCE to be received no later than July 1, 1979.

Each of these choices is more fully explained in Section III of the Federal Trade Commission's "SHOW CAUSE ORDER" which is being mailed to you. You should read this carefully.

RIGHT TO FILE A CLAIM

If you don't want to make any of the above choices, you may file a claim for whatever rights you think you have against GAC. The Trustees will still have a right to object to your claim. If such objection is filed, a hearing on the objection would be held before the Bankruptcy Court in Miami and you, or your lawyer, would then be required to prove your claim. As stated in the CLAIMS BAR ORDER which is also being mailed to you, your claim will have to be filed with the Bankruptcy Court, P.O. Box 010230, Miami Florida 33101 to be received no later than July 1. 1979. If you are unable to obtain Official Bankruptcy Form No. 15 (Proof of Claim) from a bankruptcy court, an office supply or a stationery store in your area, you may call GAC at its toll free number given below, and request a form which they will send to you.

If you have any doubts concerning this matter, the FTC recommends that you speak to an attorney to help you decide what to do. The FTC makes no recommendation whatsoever as to whether you should accept one of the choices offered under the FTC Order or whether you should file a claim instead. You, and only you, can decide whether you are better off filing a claim or accepting one of the choices under the FTC Order.

If you have any questions regarding this letter, you may direct such questions to GAC by calling its toll free number (800-327-8776) or by writing to the Federal Trade Commission/PC, Bureau of Consumer Protection, Compliance Division, Washington, D.C. 20580.

By direction of the Commission.

NOTICE OF ACCEPTANCE

____
Contract Number

I accept the following offer described in the letter sent to me by the Federal Trade Commission:

CHECK ONE

Choice No. 1:	Trustees may schedule my claim and I will deed my property to GAC	_____
Choice No. 2:	I will deed my Golden Gate Estates property to GAC in exchange for double acreage in River Ranch Acres	_____
Choice No. 3:	I will pay the $2,300 extra costs for a developed homesite in Poinciana	_____
Choice No. 4:	I will pay the $1,150 extra water and sewer betterment fees for a developed homesite in Poinciana	_____
Choice No. 5:	Within five (5) years, I have a right to contract for a GAC "Housing Construction Package"	_____

____________________ ____________________
Date Purchaser's Signature

____
Purchaser's Signature

REMEMBER: This NOTICE OF ACCEPTANCE must be received no later than July 1, 1979 by:

GAC Corporation
201 Alhambra Circle
Coral Gables, Florida 33134

APPENDIX 2

FEDERAL TRADE COMMISSION
WASHINGTON, D. C. 20580

BUREAU OF
CONSUMER PROTECTION

Dear Golden Gate Estates Customer:

As you probably know, GAC Properties, Inc. (formerly Gulf American Corporation) is in bankruptcy. In an effort to protect your interests, as much as possible, the Federal Trade Commission has entered into a new agreement with GAC. GAC's records indicate your land is located north of Stewart Boulevard in Golden Gate Estates. Stewart Boulevard is five (5) miles south of Alligator Alley (Florida State Road 858) and is one of the main east-west roads in Golden Gate Estates.

You should be aware that Golden Gate Estates will not be developed beyond the limited improvements (roads and canals) that have already been made by GAC. Collier County is now responsible for the maintenance of all roads and canals in Golden Gate Estates. Note there is no central water and sewer system. Telephone and electrical hookups may be very expensive in some isolated areas.

For lot purchasers north of Stewart Boulevard, GAC has agreed to establish an accrual Reserve Fund in the amount of $10 million dollars to be used over a period of five (5) years. All claims payable from this Reserve Fund shall be paid on a first come basis.

The purpose of this Reserve Fund is to help make sure that your property in Golden Gate Estates is suitable for homesite building. This means you should be able to install an adequate system for the disposal of sewage and have an adequate supply of potable water. The costs for obtaining electrical service to the property must be paid by the lot owner.

Under this agreement, after reorganization, you may, at your expense, have a test or tests made to determine the percolation of your land (suitability for installation of a septic tank system) and the availability of an adequate supply of potable water. The test or tests should be certified by a Registered Professional Engineer or Registered Analytical Laboratory. If the results of the test or tests indicate that the land failed to pass a percolation test or that there is no adequate supply of potable water available, these certified reports should be submitted to GAC.

PERCOLATION TEST

If your land fails to pass a percolation test, your certified report should disclose the reason for the failure, the remedial work suggested, and the estimated costs to perform the remedial work. You will be required to pay for the first $1,000 of remedial work which includes the amount you have paid for the test or tests.

If the remedial work is more than $1,000, but not more than $2,500, GAC, at its option, may: (1) pay you the excess of $1,000 or (2) request that you pay to GAC the actual cost of doing the work, up to, but not to exceed $1,000, and thereafter do the remedial work itself within sixty (60) days.

If the remedial work is more than $2,500, GAC must, within thirty (30) days after receiving such certified report or reports, exchange you into another parcel of land of equal size to your existing parcel of land and provide you with a certificate certifying the percolation of such land in its existing state without remedial work and the adequate availability of potable water as of the date of the exchange.

If GAC has no lots in its inventory which can percolate without remedial work, it may do the remedial work in order to certify both the percolation and availability of potable water and charge you for the remedial work for percolation up to $1,000 and charge you up to $500 for well drilling, less any amounts you have paid for remedial work and well drilling on your former land.

If GAC has no lots in its inventory with which to make an exchange, you will be offered a cash refund of all principal paid to GAC. When GAC makes this offer, you will also be given the choice of exchanging for land in various other GAC subdivisions with full credit for the principal and interest you have paid the company. GAC will give you full details of these various options at the time you qualify for a cash refund.

In the event of a lot exchange or refund, you will be required to deed back your land to GAC.

POTABLE WATER TEST

If you have drilled a well and your test report certifies that there is no adequate supply of potable water (as defined in the new agreement) available, GAC will have to perform such remedial work, including deeping or shallowing an existing well or drilling an additional well on the same land, and such costs shall be paid by GAC. However, if the cost of remedial work exceeds $500, GAC may exchange you into another parcel of land of equal size to your existing parcel of land and provide you with a certificate certifying the percolation of such land in its existing state without remedial work and certifying that there is an adequate supply of potable water available as of the date of the exchange.

If GAC has no lots in its inventory which can percolate with an adequate supply of potable water available without remedial work, GAC may do the remedial work in order to certify both the percolation and availability of an adequate supply of potable water and charge you for the remedial percolation work up to $1,000 and $500 for well drilling, less any amounts you have paid for such remedial percolation work and well drilling on your former land.

If GAC, has no lots in its inventory with which to make an exchange, you will be offered a cash refund of all principal paid to GAC. When GAC makes this offer, you will also be given the choice of exchanging for land in various other GAC subdivisions with full credit for the principal and interest you have paid the company. GAC will give you full details of these various options at the time you qualify for a cash refund.

In the event of a lot exchange or cash refund, you will be required to deed back your land to GAC.

RIGHT TO FILE A CLAIM

If you don't want to make any of the above choices, you may file a claim for whatever rights you think you have against GAC. The Trustees will still have a right to object to your claim. If such objection is filed, a hearing on the objection would be held before the Bankruptcy Court in Miami and you, or your lawyer, would then be required to prove your claim. As is stated in the CLAIMS BAR ORDER which is also being mailed to you, your claim will have to be filed with the Bankruptcy Court, P.O. Box 010230, Miami, Florida 33101 to be received no later than July 1, 1979. If you are unable to obtain Official Bankruptcy Form No. 15 (Proof of Claim) from a bankruptcy court, an office supply or a stationery store in your area, you may call GAC at its toll free number given below, and request a form which they will send to you.

If you have any doubts concerning this matter, the FTC recommends that you speak to an attorney to help you decide what to do. The FTC makes no recommendation whatsoever as to whether you should accept one of the

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choices offered under the FTC Order or whether you should file a claim instead. You, and only you, can decide whether you are better off filing a claim or accepting one of the choices under the FTC Order.

You should also be aware that the government of Collier County is opposed to uncontrolled development in Golden Gate Estates. In comments filed with the FTC, the county says that the roads and canals are deteriorating. The county also says that it may not spend the money necessary to maintain these structures.

If the county does decide to perform necessary maintenance the county says it may try to put the tax burden for maintenance in Golden Gate Estates on lotowners there. If the county can legally do this, taxes in Golden Gate Estates might rise.

The county is also concerned about pollution from septic tanks. The county says that if too many people try to put septic tanks in Golden Gate Estates, the county may find it necessary to make it harder to get a building permit.

The FTC cannot be sure what the county will or will not do to provide maintenance for Golden Gate Estates or to control its development.

If you have any questions regarding this letter, you may direct such questions to GAC by calling this toll free number (800-327-8776) or by writing to the Federal Trade Commission/PC, Bureau of Consumer Protection, Compliance Division, Washington, D.C. 20580.

By direction of the Commission.

APPENDIX 3

FEDERAL TRADE COMMISSION
WASHINGTON, D. C. 20580

BUREAU OF CONSUMER PROTECTION

Dear Remuda Ranch Grants Customer:

As you probably know, GAC Properties, Inc. (formerly Gulf American Corporation) is in bankruptcy. In an effort to protect your interests, as much as possible, the Federal Trade Commission has entered into a new agreement with GAC which gives you a chance to select one of three choices.

In deciding which choice you should make, you should be aware that <u>Remuda Ranch Grants will not be developed in any way</u>. <u>Most of the land in Remuda Ranch Grants is under water</u>. <u>In most areas there are no roads</u>.

<u>Choice No. 1</u>: You can deed back your land in Remuda Ranch Grants to GAC and the company will deed to you twice as much land in River Ranch Acres. <u>The land in River Ranch Acres will not be developed in any way and in most areas in River Ranch Acres there are no roads</u>. The parcels deeded to you might not be next to one another. If you are still paying for your property in Remuda Ranch Grants and you select this choice, you will still be required to make payments due on your existing contract.

<u>There is no way of knowing whether land in River Ranch has any significant value now, or will ever have any significant value</u>. There have been no sales of this land in the last few years. The land is <u>not</u> suitable for homesite use in its present condition.

<u>Choice No. 2</u>: You can exchange each 1 1/4 acres of your property in Remuda Ranch Grants for a fully developed homesite lot in Poinciana. Poinciana is a GAC homesite subdivision in central Florida. A brochure describing Poinciana has been sent to you by GAC. If you select this choice, GAC will select a lot for you, and you must pay development costs of $2,300 which may be paid at one time or paid over a seven (7) year period at 7 1/2% ANNUAL PERCENTAGE RATE. GAC advises that payment over seven (7) years will require 84 consecutive monthly payments of $35.38 each, your FINANCE CHARGE will be $671.92 on the $2,300 amount

financed, and your total of payments will be $2,971.92. In addition, regardless of whether you pay at one time or over a seven (7) year period, you will be required to pay annual property taxes plus a monthly association maintenance fee which is presently $10 per month. This association maintenance fee is a standard condition of all contracts and deeds in the Poinciana subdivision. GAC also pays annual property taxes and association maintenance fees on the property it owns in Poinciana. Of course, you will still have to pay any amount due on your existing contract.

If you pay the development costs of $2,300 all at once, you will immediately be given full title to a developed homesite lot in Poinciana, unless GAC does not have enough developed lots immediately available. GAC has over 1,000 fully developed lots available right now.

If you choose to spread your payments over time, you will not receive a deed until you are finished making all payments.

Before taking this option, you should understand that your ability to resell land in Poinciana, without a house built on the property, is uncertain at this time.

Take this option only if you want homesite property for residential use, not as an investment.

Choice No. 3: You can exchange each 2 1/2 acres of your property in Remuda Ranch Grants for a fully developed homesite lot in Poinciana which will be selected for you by GAC for an additional payment of $1,150 for water and sewer betterment fees.

This payment will be in addition to any money still due on your existing contract with GAC. You may pay this additional $1,150 at one time or it may be paid over a seven (7) year period at 7 1/2% ANNUAL PERCENTAGE RATE. GAC advises that payment over seven (7) years will require 84 consecutive monthly payments of $17.64 each, your FINANCE CHARGE will be $331.76 on the $1,150 amount financed, and your total of payments will be $1,481.76. In addition, regardless of whether you pay at one time or over a seven (7) year period, you will be required to pay annual property taxes plus a monthly association maintenance fee which is presently $10 per month. This association maintenance fee is a standard condition of all contracts and deeds in the Poinciana subdivision. GAC also pays annual property taxes and association maintenance fees on the property it owns in Poinciana.

If you pay the development costs of $1,150 all at once, you will immediately be given full title to a developed homesite lot in Poinciana, unless GAC does not have enough developed lots immediately available. GAC has over 1,000 fully developed lots available right now.

If you choose to spread your payments over time, you will not receive a deed until you are finished making all payments.

Before taking this option, you should understand that your ability to resell land in Poinciana, without a house built on the property, is uncertain at this time.

<u>Take this option only if you want homesite property for residential use, not as an investment</u>.

<u>Choice No. 4</u>: You can exchange your land for a GAC "Housing Construction Package". All of the principal and interest you have paid to GAC, limited to payments made on no more than 2 1/2 acres, will be credited to the land portion only of your "Housing Construction Package". A brochure describing GAC's present "Housing Construction Package" has been sent to you to by GAC. If you select this choice you have up to five (5) years within which to contract with GAC for a "Housing Construction Package", at the terms (including price) and conditions being offered by GAC at the time such contract is executed.

If you are still making payments on your property, you have two (2) choices if you take this option for a housing package.

--- You can stop making your payments. You will lose your land, but you will have a full credit for all the money you have paid if and when you sign a contract for a housing package. Or ....

--- You can continue to make your payments and hold onto your property. Later, if you wish, you can exchange your property for a housing package with a full credit for all the money you have paid.

If you have already fully paid for your property, you will keep it until you decide whether to exchange for a housing construction package.

This option is offered only for those who, within the next five years, want a home in Florida. As a residential investment, the value of this option is highly speculative.

To accept one of the choices listed in this letter, you must sign and return to GAC the enclosed NOTICE OF ACCEPTANCE no later than sixty (60) days after you have received this letter. If you do not answer in sixty (60) days, you will be deemed to have rejected the choices offered to you by this letter.

Each of these choices is more fully explained in Section IV of the Federal Trade Commission's "SHOW CAUSE ORDER" which is being mailed to you along with this letter. You should read this carefully.

If you have any questions regarding this letter, you may direct such questions to GAC by calling its toll free number (800-327-8776) or by writing to the Federal Trade Commission/PC, Bureau of Consumer Protection, Compliance Division, Washington, D.C. 20580.

By direction of the Commission.

NOTICE OF ACCEPTANCE

____
Contract Number

I accept the following offer described in the letter sent to me by the Federal Trade Commission:

CHECK ONE

Choice No. 1:	I will deed my Remuda Ranch Grants property to GAC in exchange for double acreage in River Ranch Acres	_____
Choice No. 2:	I will pay the $2,300 extra costs for a developed homesite in Poinciana	_____
Choice No. 3:	I will pay the $1,150 extra water and sewer betterment fees for a developed homesite in Poinciana	_____
Choice No. 4:	Within five (5) years, I have a right to contract for a GAC "Housing Construction Package"	_____

_______________ Date

_______________ Purchaser's Signature

_______________ Purchaser's Signature

REMEMBER:

This NOTICE OF ACCEPTANCE must be returned within sixty (60) days after receipt of this letter to:

GAC Corporation
201 Alhambra Circle
Coral Gables, Florida 33134

APPENDIX 4

FEDERAL TRADE COMMISSION
WASHINGTON, D. C. 20580

BUREAU OF
CONSUMER PROTECTION

Dear River Ranch Acres Customer:

As you probably know, GAC Properties, Inc. (formerly Gulf American Corporation) is in bankruptcy. In an effort to protect your interests, as much as possible, the Federal Trade Commission has entered into a new agreement with GAC which gives you a chance to select one of three choices.

In deciding which choice you should make, you should be aware that River Ranch Acres will not be developed in any way. In most areas in River Ranch Acres there are no roads.

Choice No. 1: You can get added unimproved land in River Ranch Acres which will double your holdings. Whereever possible, the additional acreage will be next to your present land. If you are still paying for your property in River Ranch Acres and you select this choice, you will still be required to make the payments due on your existing contract.

There is no sure way of knowing whether land in River Ranch has any significant value now, or will ever have any significant value. There have been no sales of this land in the last few years. The land is not suitable for homesite use in its present condition.

Choice No. 2: You can exchange each 1 1/4 acres of your property in River Ranch Acres for a fully developed homesite lot in Poinciana. Poinciana is a GAC homesite subdivision in central Florida. A brochure describing Poinciana has been sent to you by GAC. If you select this choice, GAC will select a lot for you, and you must pay development costs of $2,300 which may be paid at one time or paid over a seven (7) year period at 7 1/2% ANNUAL PERCENTAGE RATE. GAC advises that payment over seven (7) years will require 84 consecutive monthly payments of $35.38 each, your FINANCE CHARGE will be $671.92 on the $2,300 amount financed, and your total of payments will be $2,971.92. In addition, regardless of whether you pay at one time or over a seven (7) year period, you will be required to pay annual property taxes plus a monthly association maintenance fee which is presently $10 per month. This association maintenance fee is a standard condition of all contracts and deeds in the Poinciana subdivision GAC also pays annual property taxes and association maintenance fees on the property it owns in Poinciana. Of course, you will still have to pay any amount due on your existing contract.

If you pay the development costs of $2,300 all at once, you will immediately be given full title to a developed homesite lot in Poinciana, unless GAC does not have enough developed lots immediately available. GAC has over 1,000 fully developed lots available right now.

If you choose to spread your payments over time, you will not receive a deed until you are finished making all payments.

Before taking this option, you should understand that your ability to resell land in Poinciana, without a house built on the property, is uncertain at this time.

Take this option only if you want homesite property for residential use, not as an investment.

Choice No. 3: You can exchange each 2 1/2 acres of your property in River Ranch Acres for a fully developed homesite lot in Poinciana which will be selected for you by GAC for an additional payment of $1,150 for water and sewer betterment fees.

This payment will be in addition to any money still due on your existing contract with GAC. You may pay this additional $1,150 at one time or it may be paid over a seven (7) year period at 7 1/2% ANNUAL PERCENTAGE RATE. GAC advises that payment over seven (7) years will require 84 consecutive monthly payments of $17.64 each, your FINANCE CHARGE will be $331.76 on the $1,150 amount financed, and your total of payments will be $1,481.76. In addition, regardless of whether you pay at one time or over a seven (7) year period, you will be required to pay annual property taxes plus a monthly association maintenance fee which is presently

$10 per month. This association maintenance fee is a standard condition of all contracts and deeds in the Poinciana subdivision. GAC also pays annual property taxes and association maintenance fees on the property it owns in Poinciana.

If you pay the development costs of $1,150 all at once, you will immediately be given full title to a developed homesite lot in Poinciana, unless GAC does not have enough developed lots immediately available. GAC has over 1,000 fully developed lots available right now.

If you choose to spread your payments over time, you will not receive a deed until you are finished making all payments.

Before taking this option, you should understand that your ability to resell land in Poinciana, without a house built on the property, is uncertain at this time.

Take this option only if you want homesite property for residential use, not as an investment.

Choice No. 4: You can exchange your land for a GAC "Housing Construction Package". All of the principal and interest you have paid to GAC, limited to payments made on no more than 2 1/2 acres, will be credited to the land portion only of your "Housing Construction Package". A brochure describing GAC's present "Housing Construction Package" has been sent to you to by GAC. If you select this choice, you have up to five (5) years within which to contract with GAC for a "Housing Construction Package", at the terms (including price) and conditions being offered by GAC at the time such contract is executed.

If you are still making payments on your property, you have two (2) choices if you take this option for a housing package.

--- You can stop making your payments. You will lose your land, but you will have a full credit for all the money you have paid if and when you sign a contract for a housing package. Or ....

--- You can continue to make your payments and hold onto your property. Later, if you wish, you can exchange your property for a housing package with a full credit for all the money you have paid.

If you have already fully paid for your property, you will keep it until you decide whether to exchange for a housing construction package.

This option is offered only for those who, within the next five years, want a home in Florida. As a residential investment, the value of this option is highly speculative.

To accept one of the choices listed in this letter, you must sign and return to GAC the enclosed NOTICE OF ACCEPTANCE no later than sixty (60) days after you have received this letter. If you do not answer in sixty (60) days, you will be deemed to have rejected the choices offered to you by this letter.

Each of these choices is more fully explained in Section IV of the Federal Trade Commission's "SHOW CAUSE ORDER" which is being mailed to you along with this letter. You should read this carefully.

If you have any questions regarding this letter, you may direct such questions to GAC by calling its toll free number (800-327-8776) or by writing to the Federal Trade Commission/PC, Bureau of Consumer Protection, Compliance Division, Washington, D.C. 20580.

By direction of the Commission.

NOTICE OF ACCEPTANCE

____
Contract Number

I accept the following offer described in the letter sent to me by the Federal Trade Commission:

CHECK ONE

Choice No. 1: I choose to have my River Ranch Acres holdings doubled in acreage ______

Choice No. 2: I will pay the $2,300 extra costs for a developed homesite in Poinciana ______

Choice No. 3: I will pay the $1,150 extra water and sewer betterment fees for a developed homesite in Poinciana ______

Choice No. 4: Within five (5) years, I have a right to contract for a GAC "Housing Construction Package" ______

________________ ____________________
Date Purchaser's Signature

____
Purchaser's Signature

REMEMBER:

This NOTICE OF ACCEPTANCE must be returned within sixty (60) days after receipt of this letter to:

GAC Corporation
201 Alhambra Circle
Coral Gables, Florida 33134

IN THE MATTER OF

CALIFORNIA MEDICAL ASSOCIATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2967. Complaint, April 17, 1979 — Decision, April 17, 1979

This consent order, among other things, requires a San Francisco, Calif. medical association to cease publishing, promulgating, or participating in the development and use of relative value studies that set forth comparative numerical values and have the effect of establishing prices for medical and surgical services. The order further requires respondent to withdraw previously disseminated relative value studies; and send copies of the complaint and order to association members and others, together with a request for the return of all relative value studies they have in their possession.

Appearances

For the Commission: *Alfred Lindeman* and *John M. Porter.*

For the respondent: *Howard Hassard, Hassard, Bonnington, Rogers & Huber,* San Francisco, Calif.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, 15 U.S.C. 41, *et seq.,* and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that The California Medical Association has violated the provisions of Section 5 of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

PARAGRAPH 1. Respondent, California Medical Association ("CMA"), is an unincorporated association organized, existing and doing business under and by virtue of the laws of the State of California, with its principal office and place of business located at 731 Market St., San Francisco, California.

PAR. 2. CMA has approximately 25,000 members. Membership in CMA is open to doctors of medicine licensed to practice medicine in the State of California, persons within the State of California who have retired from the practice of medicine, persons distinguished for their services or attainments as doctors of medicine or in the field of public health, or for research or other scientific work contributing to medicine, and persons within certain other special and limited classes established by CMA.

Many members of CMA are licensed physicians engaged in the private practice of medicine and surgery and derive substantial portions of their professional income from fees for medical and surgical procedures charged directly to patients or to insurers.

PAR. 3. The acts and practices of CMA are in or affect commerce as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. Since 1956, CMA has, on various occasions, prepared, published, and circulated to its members and others "relative value studies" which set forth in non-monetary units comparative numerical values for procedures performed and services rendered by physicians and other health care providers. Each value is convertible into a monetary fee by the application of a dollar conversion factor to the basic unit. Said "relative value studies" include detailed instructions for the computation and use of conversion factors to determine physicians' fees. Said "relative value studies" have been widely disseminated and used as the basis of fee schedules by physicians and other health care providers both within and outside the state of California.

PAR. 5. The preparation, publication, and circulation by CMA of relative value studies have the effect of establishing, maintaining, or otherwise influencing the fees which physicians and other health care providers charge for their professional services and are in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the San Francisco Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent California Medical Association is an unincorporated association organized, existing and doing business under and by virtue of the laws of the State of California, with its principal offices located at 731 Market St., San Francisco, California.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

I

A. The term "relative value study" means any list of compilation of medical procedures and/or services which sets forth comparative numerical values for such procedures performed and/or services rendered by physicians and other health care providers, without regard to whether those values are expressed in monetary or non-monetary terms.

B. The term "CMA" means the California Medical Association.

C. The term "component" means a county or district medical society chartered by CMA.

D. The term "conversion factor" means any monetary value multiplier used or intended to be used to convert non-monetary values in a relative value study to monetary fees.

E. The term "third party" means any organization which is or may be required by contract or statute to pay or reimburse the whole or any part of any financial obligation for health care incurred by any recipient of such care.

F. The term "historical data" means complete and unprocessed responses obtained from surveying fees charged for procedures performed and/or services rendered by physicians or other health care providers, accurate tabulated summaries of such responses, or accurate statistical representations of such responses such as arithmetic means, medians or percentiles.

G. The term "effective date of this order" means the date of service of this order.

II

It is ordered, That CMA, its successors, or assigns, and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division, or other device, shall:

A. Cease and desist from directly or indirectly initiating, originating, developing, publishing, or circulating the whole or any part of any proposed or existing relative value study;

B. Cease and desist from directly or indirectly suggesting or instructing that conversion factors may be computed and applied to the relative value units contained in any relative value study.

C. Cease and desist from directly or indirectly advising in favor of or against the use of, or contributing to, the whole or any part of any proposed or existing relative value study. It shall not be considered a violation of this paragraph, however, for CMA to furnish testimony, information or advice to any government body, committee, or instrumentality, or to furnish to any third party such information as may be requested, relating to the use by such government entity or third party of the whole or part of any relative value study for purposes of establishing payment, compensation or reimbursement levels to be made to physicians or other health care providers by such government entity or third party; provided that any information furnished by CMA which may bear directly or indirectly on compensation levels for procedures performed and/or services rendered by physicians or other health care providers shall be limited to historical data, as defined herein, and shall be completely described as to methodology.

D. Permanently cancel, repeal, abrogate, and withdraw any and all relative value studies which it has heretofore developed, published, circulated, or disseminated; *provided, however,* that nothing contained in this order shall prohibit CMA from initiating, originating, developing, publishing, circulating, adopting, contributing to, recommending, suggesting, or advising in favor of or against the use of any list or compilation of standardized terminology describing procedures performed and/or services rendered by physicians and other health care providers, so long as such list or compilation does not directly or indirectly set forth absolute or comparative numerical values for any such procedures or services.

E. Within thirty (30) days after the effective date of this order, distribute by first class mail a copy of the Commission's complaint and order in this matter, as well as a letter, in the form shown in

Appendix "A" to this order, to each of its members, to each state medical association known to CMA to have received from it the 1974 edition of the California Relative Value Studies, and to each of its components, third-party payers and others listed in Appendix "B" to this order, notifying such members, associations, components, third-party payers and others to return to CMA all copies of CMA relative value studies in their possession. Except for printing and mailing costs, CMA is not obligated to incur any expense under this paragraph.

III

It is further ordered, That CMA notify the Commission at least thirty (30) days prior to any proposed change in its organization which might affect compliance obligations under this order, such as, but not limited to, dissolution, the emergence of a successor association or corporation, and the creation and/or dissolution of subsidiaries.

IV

It is further ordered, That CMA shall, within sixty (60) days after service upon it of this order, file with the Commission a report in writing, setting forth in detail the manner and form in which it has complied with this order.

V

Nothing in this order shall be construed to exempt CMA from complying with the antitrust laws or the Federal Trade Commission Act. The fact that any activity is not prohibited by this order shall not bar a challenge to it under such laws.

APPENDIX A

(CMA LETTERHEAD)

TO: Recipients of CMA Relative Value Studies

As you may be aware, the FTC has been investigating various components of health care, including relative value study activities of CMA. The Association no longer desires to continue such activities and has discontinued them. It has entered into an agreement with the Federal Trade Commission to formalize the discontinuance of its relative value studies.

This agreement resulted in the issuance by the Federal Trade Commission on _______________ of a complaint and the entry of a consent order which requires, in essence, that CMA:

(a) stop publishing and participating in the development of relative value studies;
(b) withdraw the relative value studies it has already published;
(c) stop suggesting and instructing that conversion factors may be computed and applied to units contained in relative value studies;
(d) distribute a copy of the complaint and consent order to CMA relative value study recipients; and
(e) notify recipients of CMA's relative value studies to return them to CMA.

The complaint alleges basically that CMA's relative value studies have the effect of influencing fees charged by physicians. The consent agreement with the FTC states that it is for settlement purposes only and does not constitute an admission by the CMA of the charges in the complaint or that the law has been violated.

In accordance with the provisions of the FTC's order, you are to cease using and to return all copies of any CMA relative value study in your possession.

The proper mailing address:

California Medical Association
731 Market Street
San Francisco, California 94103

Copies of the FTC's complaint and order are enclosed.

Sincerely,

____

President

Enclosures

APPENDIX "B"

Commissioner
Medical Services Administration
Social and Rehabilitation Service
Department of Health, Education, and Welfare
330 C Street, S.W.
Washington, DC 20201

Commissioner of Social Security
Department of Health, Education, and Welfare
6401 Security Boulevard
Baltimore, MD 21235

National Association of Blue Shield Plans
211 East Chicago Avenue
Chicago, IL 60611

Deputy Assistant Secretary for Health Resources and Programs
Department of Defense
Washington, DC 20301

Directorate
OCHAMPUS
Department of Defense
Washington, DC 20301

OCHAMPUS
Department of Defense
Denver, CO 80240

Health Application Systems
1633 Bayshore Highway
Burlingame, CA 94010

Blue Cross of Southern California
Box 27747
4777 Sunset Boulevard
Los Angeles, CA 90027

Blue Cross and Blue Shield of Alabama
930 S. 20th Street
Birmingham, AL 35298

Blue Cross of Northern California
1950 Franklin Street
Oakland, CA 94659

Blue Cross of Arizona, Inc.
321 W. Indian School Road
Box 13466
Phoenix, AZ 85002

Blue Shield of California
2 North Point
San Francisco, CA 94113

Arizona Blue Shield Medical Service
321 W. Indian School Road
Box 13466
Phoenix, AZ 85002

Colorado Hospital Service - BC
244 University Boulevard
Denver, CO 80206

Arkansas Blue Cross and Blue Shield, Inc.
601 Gaines Street
Box 2181
Little Rock, AR 72203

Colorado Medical Service, Inc. - BS
244 University Boulevard
Denver, CO 80206

Connecticut Medical Service, Inc.
221 Whitney Avenue
New Haven, CT 06509

Connecticut Blue Cross, Inc.
Box 504
370 Bassett Road
North Haven, CT 06473

Blue Cross and Blue Shield of Delaware, Inc.
201 W. 14th Street
Box 1991
Wilmington, DE 19899

Hawaii Medical Service Association
1504 Kapiolani Boulevard
Box 860
Honolulu, HI 96808 - BS

Group Hospitalization, Inc. - BC
550 12th Street, S.W.
Washington, DC 20024

Blue Cross of Idaho, Inc.
1501 Federal Way
Box 7408
Boise, ID 83707

Medical Service of the District of Columbia - BS
550 12th Street, S.W.
Washington, DC 20024

North Idaho District Medical Service Bureau, Inc. - BS
1602 21st Avenue
Box 1106
Lewiston, ID 83501

Blue Cross of Florida, Inc.
532 Riverside Avenue
Box 1798
Jacksonville, FL 32201

Illinois Hospital and Health - BC Service, Inc.
227 N. Wyman Street
Rockford, IL 61101

Blue Shield of Florida, Inc.
532 Riverside Avenue
Box 1798
Jacksonville, FL 32201

Blue Cross of Georgia/Atlanta Inc.
1010 West Peachtree St., N.W.
Box 4445
Atlanta, GA 30302

Blue Cross of Georgia/Columbus Inc.
2357 Warm Springs Road
Box 1520
Columbus, GA 31902

Blue Shield of Georgia/Atlanta Inc.
1010 West Peachtree St., N.W.
Box 4445
Atlanta, GA 30302

Blue Shield of Georgia/Columbus Inc.
2357 Warm Springs Road
Box 1520
Columbus, GA 31902

Blue Shield of Iowa
Liberty Building
Des Moines, IA 50307

Kansas Hospital Service Association, Inc.
1133 Topeka Avenue
Box 239
Topeka, KS 66601

Kansas Blue Shield
1133 Topeka Avenue
Box 239
Topeka, KS 66601

Blue Cross Hospital Plan Inc.
3101 Bardstown Road
Louisville, KY 40205

Kentucky Physicians' Mutual, Inc.
3101 Bardstown Road
Louisville, KY 40205

Blue Cross of Louisiana
10225 Florida Boulevard
Box 15699
Baton Rouge, LA 70815

Hospital Service Corporation - BC
233 North Michigan Avenue
Box 1364
Chicago, IL 60601

Illinois Medical Service - BS
233 North Michigan Avenue
Chicago, IL 60601

Blue Cross of Indiana
120 W. Market Street
Indianapolis, IN 46204

Mutual Medical Insurance Inc. - BS
120 W. Market Street
Indianapolis, IN 46204

Blue Cross of Iowa
Liberty Building
Sixth Street & Grand Avenue
Des Moines, IA 50307

Blue Cross of Michigan
600 Lafayette E.
Detroit, MI 48226

Blue Shield of Michigan
600 Lafayette E.
Detroit, MI 48226

Blue Cross and Blue Shield of Minnesota
3535 Blue Cross Road
Box 3560
St. Paul, MN 55165

Blue Cross and Blue Shield of Minnesota
2344 Nicollet Avenue
Minneapolis, MN 55404

Blue Cross and Blue Shield of Mississippi, Inc.
530 E. Woodrow Wilson Drive
Box 1043
Jackson, MS 39205

Blue Cross of Kansas City
3637 Broadway
Box 169
Kansas City, MO 64141

Hospital Service Association of New Orleans - BC
2026 St. Charles Avenue
New Orleans, LA 70130

Maine Blue Cross and Blue Shield
110 Free Street
Portland, ME 04101

Blue Cross of Maryland
700 E. Joppa Road
Box 9836
Towson, MD 21204

Blue Shield of Maryland, Inc.
700 E. Joppa Road
Towson, MD 21204

Blue Cross of Massachusetts
133 Federal Street
Boston, MA 02106

Blue Cross and Blue Shield of South Carolina
I-20 East at Alpine Road
Columbia, SC 29219

Blue Cross of Western Iowa and South Dakota
Third & Pierce Streets
Box 1677
Sioux City, IO 51102

South Dakota Medical Service, Inc.
711 N. Lake Avenue
Sioux Falls, SD 57104

Blue Cross-Blue Shield of Tennessee
801 Pine Street
Chattanooga, TN 37402

Kitsap Physicians' Service
820 Pacific Avenue
Box 339
Bremerton, WA 98310

Blue Cross Hospital Service, Inc.
Commerce Square
Box 1343
Charleston, WV 25325

Blue Cross Hospital Service, Inc. of Missouri
1430 Olive Street
St. Louis, MO 63103

Blue Shield of Kansas City
3637 Broadway
Box 169
Kansas City, MO 64141

St. Louis Blue Shield
5775 Campus Parkway
Hazelwood, MO 63042

Blue Cross of Montana
3360 10th Avenue S.
Great Falls, MT 59405

Montana Physicians' Service - BS
404 Fuller Avenue
Box 1677
Helena, MT 59601

Blue Cross of Virginia
2015 Staples Mill Road
Box 27401
Richmond, VA 23279

Blue Cross of Southwestern Virginia
1212 Third Street, S.W.
Box 2770
Roanoke, VA 24001

Blue Shield of Virginia
2015 Staples Mill Road
Box 27401
Richmond, VA 23279

Blue Shield of Southwestern Virginia
1212 Third Street, S.W.
Box 2770
Roanoke, VA 24001

Associated Hospitals, Inc.
401 Federal Street
Box 131
Bluefield, WV 24701

Parkersburg Hospital Service, Inc.
203 Union Trust Building
Box 1948
Parkersburg, WV 26101

West Virginia Hospital Service, Inc.
20th & Chapline Streets
Wheeling, WV 26003

Surgical Service, Inc.
Commercial Bank Building
Box 131
Bluefield, WV 24701

Blue Shield of Southern West Virginia, Inc.
Commerce Square
Box 1353
Charleston, WV 25325

Medical-Surgical Service, Inc.
Union National Bank Building
Clarksburg, WV 26301

Morgantown Medical-Surgical Service, Inc.
265 High Street
Morgantown, WV 26505

Memphis Hospital Service and Surgical Association, Inc.
85 N. Danny Thomas Boulevard
Box 98
Memphis, TN 38101

West Virginia Medical Service Inc.
20th & Chapline Streets
Box 6246
Wheeling, WV 26003

Group Hospital Service, Inc.
Main at N. Central Expressway
Dallas, TX 75201

Associated Hospital Service, Inc.
4115 N. Teutonia Avenue
Box 2025
Milwaukee, WI 53201

Group Life and Health Insurance Co.
Main at N. Central Expressway
Dallas, TX 75201

Wisconsin Physicians' Service
330 E. Lakeside Street
Box 1109
Madison, WI 53701

Blue Cross of Utah
2455 Parley's Way
Box 270
Salt Lake City, UT 84110

Surgical Care, The Blue Shield Plan of the Medical Society of Milwaukee County
756 N. Milwaukee Street
Milwaukee, WI 53202

Blue Shield of Utah
2455 Parley's Way
Box 270
Salt Lake City, UT 84110

Blue Cross of Wyoming
4020 House Avenue
Box 2266
Cheyenne, WY 82001

Blue Shield of Wyoming
4020 House Avenue
Box 2266
Cheyenne, WY 82001

Genesee Valley Medical Care, Inc.
41 Chestnut Street
Rochester, NY 14647

Medical Mutual of Cleveland, Inc.
2060 E. Ninth Street
Cleveland, OH 41115

Blue Shield of Central New York, Inc.
344 S. Warren Street
Syracuse, NY 13202

Ohio Medical Indemnity, Inc.
6740 N. High Street
Worthington, OH 43085

Medical and Surgical Care, Inc.
5 Hopper Street
Utica, NY 13501

Blue Cross and Blue Shield of North Carolina
P. O. Box 2291
1830 Chapel Hill-Durham Blvd.
Durham, NC 27702

Blue Cross of North Dakota
301 S. Eighth Street
Fargo, ND 58102

Blue Shield of North Dakota
301 S. Eighth Street
Fargo, ND 58102

Blue Cross Hospital Plan, Inc.
201 Ninth Street, N.W.
Canton, OH 44702

Blue Cross of Southwest Ohio
1351 William Howard Taft Rd.
Cincinnati, OH 45206

Blue Cross of Northeast Ohio
2066 E. Ninth Street
Cleveland, OH 44115

Blue Cross of Central Ohio
174 E. Long Street
Columbus, OH 43215

Blue Cross of Lima, Ohio
7 Public Square
Box 1046
Lima, OH 45802

Blue Cross of Northwest Ohio, Inc.
3737 Sylvania Avenue
Box 943
Toledo, OH 43656

Blue Cross of Nebraska
Box 3248
Main P.O. Station
Omaha, NB 68103

Blue Cross and Blue Shield of Oklahoma
1215 S. Boulder Avenue
Box 3283
Tulsa, OK 74102

Blue Cross of Oregon
100 S.W. Market Street
Box 1271
Portland, OR 97207

Oregon Physicians' Service
619 S.W. 11th Avenue
Box 1071
Portland, OR 97207

Blue Cross of Lehigh Valley
1221 Hamilton Street
Allentown, PA 18102

Capital Blue Cross
100 Pine Street
Harrisburg, PA 17101

Blue Cross of Greater Philadelphia
1333 Chestnut Street
Philadelphia, PA 19107

Blue Cross of Western Pennsylvania
1 Smithfield Street
Pittsburgh, PA 15222

Blue Cross of Northeastern Pennsylvania
15 S. Franklin Street
Wilkes-Barre, PA 18701

Pennsylvania Blue Shield
Blue Shield Building
Camp Hill, PA 17011

Blue Cross and Blue Shield of Rhode Island
Box 1298
444 Westminster Mall
Providence, RI 02901

Chautauqua Region Hospital Service Corporation
306 Spring Street
Box 1119
Jamestown, NY 14701

Blue Shield of Nebraska
Box 3248
Main P.O. Station
Omaha, NB 68103

Nevada Blue Shield
3660 Baker Lane
Reno, NV 89502

New Hampshire-Vermont Hospitalization Service - BC
2 Pillsbury Street
Concord, NH 03301

New Hampshire-Vermont Physicians' Service
2 Pillsbury Street
Concord, NH 03301

Hospital Service Plan of New Jersey - BC
33 Washington Street
Box 420
Newark, NJ 07101

Medical-Surgical Plan of New Jersey - BS
33 Washington Street
Newark, NJ 07102

New Mexico Blue Cross and Blue Shield, Inc.
12800 Indian School Road N.E.
Albuquerque, NM 87112

Blue Cross of Northeastern New York, Inc.
1251 New Scotland Road
Box 8650
Albany, NY 12208

Blue Cross of Western New York, Inc.
298 Main Street
Buffalo, NY 14202

Blue Cross of Washington-Alaska, Inc.
15700 Dayton Avenue, North
Seattle, WA 98133

The Indiana State Medical Association
3935 North Meridian Street
Indianapolis, IN 46208

Associated Hospital Service of New York
622 Third Avenue
New York, NY 10017

Rochester Hospital Service Corporation
41 Chestnut Street
Rochester, NY 14647

Blue Cross of Central New York, Inc.
344 S. Warren Street
Box 271
Syracuse, NY 13201

Hospital Plan, Inc.
5 Hopper Street
Utica, NY 13501

Hospital Service Corporation of Jefferson County
158 Stone Street
Watertown, NY 13601

Blue Shield of Northeastern New York, Inc.
Box 8650
Albany, NY 12208

Blue Shield of Western New York, Inc.
298 Main Street
Buffalo, NY 14202

Chautauqua Region Medical Service Inc.
306 Spring Street
Jamestown, NY 14701

United Medical Service, Inc.
2 Park Avenue
New York, NY 10016

California Physicians' Service
P. O. Box 7608
San Francisco, CA 94120

Colorado Medical Service, Inc.
244 University Blvd.
Denver, CO 80206

Continental Service Life
& Health Insurance Company
Box 3397
5353 Florida Boulevard
Baton Rouge, LA 70821

Connecticut General Life
Insurance Company
Hartford, CT 06115

Blue Cross & Blue Shield of Greater
New York
622 3rd Avenue
New York, NY 10016

Medical Association of Georgia
938 Peachtree Street, N.E.
Atlanta, GA 30309

Missouri Medical Service
5775 Campus Parkway
Hazelwood, MO 63042

Mississippi State Medical Association
735 Riverside Drive
Jackson, MS 39216

Washington Physicians' Service
220 West Harrison Street
Seattle, WA 98119

Medical-Surgical Care, Inc.
203 Union Trust Building
Box 1948
Parkersburg, WV 26101

New York Life Insurance Company
51 Madison Avenue
New York, NY 10010

Metropolitan Life Insurance Company
1 Madison Avenue
New York, NY 10010

Prudential Insurance Company of America
Prudential Plaza
Newark, NJ 07101

The Travelers Insurance Company
1 Tower Square
Hartford, CT 06115

Continental Assurance Company
CNA Plaza
Chicago, IL 60605

Aetna Life Insurance Company
151 Farmington Avenue
Hartford, CT 06115

Bankers Life Company
711 High Street
Des Moines, IA 50307

Employers Life Insurance Company of
Wausau
2000 Westwood Drive
Wausau, WI 54401

Nationwide Life Insurance Company
246 North High Street
Columbus, OH 43216

Colonial Penn Life Insurance Company
5 Penn Center Plaza
Philadelphia, PA 19103

Equitable Life Assurance Society of the
U.S.
1285 Avenue of the Americas
New York, NY 10019

Firemen's Fund Insurance Company
3333 California Street
San Francisco, CA 94118

Reliance Insurance Group
4 Penn Center Plaza
Philadelphia, PA 19103

Zurich Life Insurance Company
111 West Jackson Boulevard
Chicago, IL 60604

Occidental Life Insurance
Company of California
Box 2101 Terminal Annex
Los Angeles, CA 90054

Mutual of Omaha Insurance Company
Dodge at 33rd Street
Omaha, NE 68131

Blue Shield of Massachusetts, Inc.
133 Federal Street
Boston, MA 02106

Blue Cross of Eastern Ohio, Inc.
2400 Market Street
Youngstown, OH 44507

Nevada State Medical Association
3660 Baker Lane
Reno, NV 89502

Alameda-Contra Costa Medical Association
6230 Claremont Avenue
Oakland, CA 94618

Butte-Glenn Medical Society
811 East Fifth Avenue
Chico, CA 95926

Butte-Glenn Foundation for Medical Care
815 East Fifth Avenue
Chico, CA 95926

Forty First Medical Society
3250 Wilshire Boulevard
Suite 606
Los Angeles, CA 90010

Fresno-Madera Medical Society
P. O. Box 31
Fresno, CA 93707

Foundation for Medical Care of Fresno County
P. O. Box 31
Fresno, CA 93707

Humboldt-Del Norte County Medical Society
P. O. Box 1395
3100 Edgewater Drive
Eureka, CA 95501

Humboldt-Del Norte Foundation for Medical Care
P. O. Box 1395
Eureka, CA 95501

Imperial County Medical Society
200 South Imperial Avenue
Imperial, CA 92251

Inyo-Mono County Medical Society
c/o Owen R. Walker, MD, President
293 Willow Street
Bishop, CA 93514

Kern County Medical Society
1314 17th Street
Bakersfield, CA 93301

Foundation for Medical Care of Kern County
2603 G Street
Bakersfield, CA 93301

Kings County Medical Society
P. O. Box 1003
Hanford, CA 93230

Lassen-Plumas-Modoc-Sierra County Medical Society
c/o Herman H. Gray, MD, President
P. O. Box 519
Chester, CA 96020

Los Angeles County Medical Association
P. O. Box 3465
Terminal Annex
Los Angeles, CA 90054

Marin Medical Society
P. O. Box 4344
4460 Redwood Highway
San Rafael, CA 94903

Marin Foundation for Medical Care, Inc.
P. O. Box 4344
San Rafael, CA 94903

Mendocino-Lake County Medical Society
P. O. Box 722
215 West Standley Drive
Ukiah, CA 95482

Merced-Mariposa Medical Society
2835 North G Street
Merced, CA 95340

Foundation for Medical Care of Merced County
2835 G Street
Bear Creek Plaza
Merced, CA 95340

Monterey County Medical Society
P. O. Box 308
19045 Portola Drive
Salinas, CA 93901

Monterey Bay Area Foundation for Medical Care
P. O. Box 308
Salinas, CA 93901

Napa County Medical Society
1041 Lincoln Avenue
P. O. Box 2158
Napa, CA 94558

Orange County Medical Association
300 South Flower Street
Orange, CA 92668

Foundation for Medical Care of Orange County
300 South Flower Street
Orange, CA 92668

Placer-Nevada County Medical Society
1212 High Street
Auburn, CA 95603

Riverside County Medical Association
6833 Indiana Avenue
Riverside, CA 92506

Foundation for Medical Care of Riverside County
6833 Indiana Avenue
Riverside, CA 92506

Sacramento County Medical Society
5380 Elvas Avenue
Sacramento, CA 95819

Medical Care Foundation
650 University Avenue
Sacramento, CA 95825

San Benito County Medical Society
c/o Fisk Brooks, MD, President
565 Monterey Street
Hollister, CA 95023

San Bernardino County Medical Society
P. O. Box 5216
San Bernardino, CA 92412

San Bernardino Foundation for Medical Care
P. O. Box 6186
San Bernardino, CA 92412
San Diego, CA 92123

San Diego County Medical Society
P. O. Box 23015
3702 Ruffin Road

San Diego Foundation for Medical Care
3702 Ruffin Road
San Diego, CA 92123

San Francisco Medical Society
250 Masonic Avenue
San Francisco, CA 94118

San Francisco Medical Society Health Plan, Inc.
250 Masonic Avenue
San Francisco, CA 94118

San Joaquin Foundation for Medical Care
P. O. Box 230
Stockton, CA 95203

Medical Care Foundation of
/Santa Barbara County
Nine East Pedrogosa
Santa Barbara, CA 93101

The Health Care Foundation
of San Mateo County, Inc.
3080 La Selva
San Mateo, CA 94403

Medical Care Foundation
of Santa Barbara County
Nine East Pedrogosa
Santa Barbara, CA 93101

Foundation for Medical Care
of Santa Clara County
P. O. Box 50003
San Jose, CA 95150

Monterey Bay Area Foundation for Medical Care
P. O. Box 308
Salinas, CA 93901

Siskiyou County Medical Society
c/o Donald Meamber, MD, President
750 South Main
Yreka, CA 96097

Sonoma County Medical Association
3452 Mendocino Avenue
Santa Rosa, CA 95401

Stanislaus Medical Society
P. O. Box 1755
Modesto, CA 95354

Tehema County Medical Society
343 Oak Street
Red Bluff, CA 96080

San Joaquin County Medical Society
P. O. Box 230
445 West Acacia Street
Stockton, CA 95201

San Luis Obispo County Medical Society
P. O. Box 319
San Luis Obispo, CA 93406

San Mateo County Medical Society
3080 La Selva
San Mateo, CA 94403

Medical Society of Santa Barbara County
Nine East Pedrogosa
Santa Barbara, CA 93101

Santa Clara County Medical Society
700 Empey Way
San Jose, CA 95128

Santa Cruz County Medical Society
P. O. Box 308
Salinas, CA 93901

Shatsa-Trinity County Medical Society
P. O. Box 959
Redding, CA 96001

Solano County Medical Society
773 Tuolumne Street
Vallejo, CA 94590

Foundation for Medical Care of Sonoma County
3452 Mendocino Avenue
Santa Rosa, CA 95401

Stanislaus Foundation for Medical Care
P. O. Box 1755
Modesto, CA 95354

Tulare County Medical Society
P. O. Box 16
1821 West Meadow Lane
Visalia, CA 93277

Foundation for Medical Care of Tulare County
1821 West Meadow Lane, Suite A
Visalia, CA 93277

Ventura County Medical Society
2977 Loma Vista Road
Ventura, CA 93003

Ventura County Foundation for Medical Care
3212 Loma Vista Road
Ventura, CA 93003

Yolo County Medical Society
P. O. Box 1312
117 West Main Street, Suite 20
Woodland, CA 95695

Medical Care Foundation
650 University Avenue
Sacramento, CA 95825

Yuba-Sutter-Colusa County Medical Society
P. O. Box L
Marysville, CA 95901

Los Angeles County Medical Association
District 1 - Metropolitan
1925 Wilshire Boulevard
Los Angeles, CA 90057

Los Angeles County Medical Association
District 2 - Pasadena
127 North Madison Ave., Suite 110
Pasadena, CA 91101

Los Angeles County Medical Association
District 3 - Long Beach
115 East Eighth Street
Long Beach, CA 90813

Long Beach Foundation for Medical Care
P. O. Box 887
Long Beach, CA 90813

Los Angeles County Medical Association
District 4 - Glendale
545 West Glenoaks Boulevard
Glendale, CA 91202

Los Angeles County Medical Association
District 5 - Bay
2901 Wilshire Blvd., Suite 101
Santa Monica, CA 90403

Los Angeles County Medical Association
District 6 - West San Fernando Valley
15910 Ventura Blvd., Suite 1403
Encino, CA 91436

San Fernando Valley Foundation for Medical Care
15910 Ventura Boulevard
Encino, CA 91436

Los Angeles County Medical Association
District 7 - Beverly Hills
184 North Canon Drive
Beverly Hills, CA 90210

Los Angeles County Medical Association
District 8 - South
438 South Gaffey
San Pedro, CA 90731

Los Angeles County Medical Association
District 9 - Southwest
3655 Lomita Blvd., Suite 319
Torrance, CA 90505

Los Angeles County Medical Association
District 10 - Southeast
14724 Ventura Blvd., Suite 604
Sherman Oaks, CA 91403

Los Angeles County Medical Association
District 11 - East
13766 East Philadelphia Street
Whittier, CA 90601

Los Angeles County Medical Association
District 12 - San Gabriel Valley
P. O. Box 848
San Gabriel, CA 91778

Los Angeles County Medical Association
District 13 - Foothill
735 West Duarte Road, Suite 405
Arcadia, CA 91006

Los Angeles County Medical Association
District 14 - Pomona
1798 North Garey Avenue
Pomona, CA 91767

Los Angeles County Medical Association
District 15 - Centinela Valley
P. O. Box 2368
Inglewood, CA 90305

Los Angeles County Medical Association
District 16 - Antelope Valley
P. O. Box 2469
Lancaster, CA 93534

Los Angeles County Medical Association
District 17 - East San Fernando Valley
14724 Ventura Blvd., Suite 604
Sherman Oaks, CA 91403

IN THE MATTER OF

INTERMATIC INCORPORATED

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2961. Complaint, April 25, 1979 — Decision, April 25, 1979

This consent order, among other things, requires a Spring Grove, Ill. manufacturer and distributor of electrical devices to cease misrepresenting energy or cost savings that may be realized through the use of its water heater timer without disclosing that use of the timer would decrease the quantity and temperature of hot water used and adversely affect dishwasher operations. The firm would be required to make relevant disclosure statements in product advertising, labeling and instructions; and recall all previously disseminated material which fails to conform with the terms of the order. Additionally, the firm would be required to continue its existing refund policy; and maintain specified records for designated time periods.

Appearances.

For the Commission: *Randall H. Brook* and *Michael E. Kipling.*

For the respondent: *Ann Ray Heitland* and *Richard J. Hoskins, Schiff, Hardin & Waite,* Chicago, Ill.

COMPLAINT

The Federal Trade Commission, having reason to believe that Intermatic Incorporated, a corporation, has violated Section 5 of the Federal Trade Commission Act, as amended, and that a proceeding in that respect is in the public interest, issues this complaint.

PARAGRAPH 1. Respondent Intermatic Incorporated ("Intermatic") is a Delaware corporation with its principal office and place of business at Intermatic Plaza, Spring Grove, Illinois.

Allegations below stated in the present tense include the past tense.

PAR. 2. Intermatic is engaged in the manufacture, advertising, offering for sale, sale and distribution of a variety of electric appliances (primarily electric timing and switching devices) for home and business usage.

PAR. 3. In the conduct of its business, Intermatic ships electric appliances and devices to wholesale purchasers throughout the United States. Intermatic prepares advertising, promotional and labeling materials for its products in Spring Grove, Illinois and disseminates these materials throughout the country. Intermatic, therefore, maintains a substantial course of advertising and trade in electric appliances and devices in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 4. In the course of its business, Intermatic has advertised and sold an "electric water heater timer," and electric appliance or device designed for permanent installation in electrical circuits supplying home water heaters. The timer is identical in function to standard electric 24-hour clock timers (*i.e.*, those not designated as "water heater timers"). The timer can be set to turn on and off the power supplied to the water heater at various preset times during each 24-hour period.

PAR. 5. Intermatic's advertising for its electric water heater timer suggests using it to turn on the heater for a one-hour period in the morning and for a two-hour period in the evening during "periods of major hot water usage."

PAR. 6. Intermatic represents, directly or by implication, that:

A. Use of the timer will result in substantial savings on water heating bills without significant reduction in hot water usage or change in lifestyle. Expected annual savings range in amount from $48 to $120. Electric water heating costs are expected to diminish by an average of 35 percent because of the timer.

B. Cost savings are attributable to saving energy which is used by a water heater during periods when no hot water is being drawn off.

C. Intermatic has a reasonable basis in valid scientific studies or tests from which to conclude that substantial or specific cost savings will be realized by typical consumers using its timer without significant reduction in hot water usage.

PAR. 7. Contrary to these representations:

A. The use of a water heater timer will not result in substantial savings on water heating bills, nor in the specific dollar or percentage savings claimed by Intermatic, without a significant reduction in both the quantity and temperature of hot water used.

B. Any savings actually attributable to "off" periods will be negligible, since any heat lost during "off" periods must be made up by additional energy consumption during "on" periods. The only substantial savings occur from consumer acceptance of lower temperature and quantity of hot water.

C. Intermatic did not have a reasonable basis in valid scientific studies or tests from which to conclude that its representations were true.

PAR. 8. In actual use as suggested by Intermatic's instructions, hot water temperature may drop thirty to forty degrees or more. Consumers may be unaware that water temperature is inadequate for some uses, particularly to meet recommended minimum temperatures for dishwashers.

PAR. 9. The misrepresentations by Intermatic have the tendency and capacity to induce consumers to purchase the water heater timer based on the incorrect belief that substantial savings may be realized without reduction in hot water usage.

PAR. 10. The fact that the temperature of hot water available to consumers is much lower when the water heater timer is used and the fact that consumers who use the timer may be forced to schedule certain activities (*e.g.*, dishwashing) at specific times of the day when adequate hot water is available are facts material in light of consumers' understanding of the function and use of the timer. Failure to disclose these material facts has the tendency and capacity to mislead consumers to purchase the timer based on the incorrect belief that substantial savings may be realized without reduction in hot water usage and that substantial savings may be realized without changing one's lifestyle.

PAR. 11. Many of the purchasers of Intermatic's water heater timer may incur additional, often greater, expense in paying for installation of the device by a licensed electrician. Consumers could realize savings equal to or greater than those claimed by simply turning down water heater thermostats and/or reducing hot water usage. PAR. 12. The use of the water heater timer could be of harm to some electrical generation programs by public and private utilities. By maximizing water heater usage during peak energy consumption periods of the day, as directed by Intermatic, additional strains will be put on some power generating facilities at the hours when they are already most heavily taxed. The result of increased peak hour load usage is that utilities will have to rely on their oldest or most expensive back-up generation systems to meet the peaks. This will increase costs to the consumers and the public as a whole. On a long range basis, it may further increase public costs by contributing to the need for new generator facilities.

The promotion and sale of the water heater timer to be used as directed is contrary to public policy and therefore unfair.

PAR. 13. For the reasons stated above, and because sale of the timers may divert consumer expenditures away from valid energy saving methods, including insulating water heaters and pipes, the acts and practices of Intermatic are to the prejudice and injury of the public and constitute false, misleading, deceptive and unfair acts or

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practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.

Decision and Order

The Federal Trade Commission has initiated an investigation of certain acts and practices of respondent Intermatic Incorporated. The respondent has been furnished with a copy of a draft complaint which the Seattle Regional Office proposed to present to the Commission for its consideration. If issued by the Commission, this complaint would charge respondent with violation of the Federal Trade Commission Act.

Respondent, its attorney, and counsel for the Commission have executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts in the complaint, and a statement that the signing of the agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in the complaint. The agreement also includes waivers and other provisions as required by the Commission's Rules.

The Commission has considered the matter and has determined that it has reason to believe that the respondent has violated the Federal Trade Commission Act, and that the complaint should issue. The Commission has therefore accepted the executed consent agreement and placed the agreement on the public record for a period of sixty (60) days. Now, in conformance with Section 2.34 of its Rules, the Commission issues the complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Intermatic Incorporated is a Delaware corporation with its office and principal place of business at Intermatic Plaza, Spring Grove, Illinois.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

This order applies to respondent Intermatic Incorporated ("Intermatic"), its successors, assigns, officers, agents and employees, whether acting directly or through any corporation, subsidiary, division or other device. Order provisions apply to any acts taken in connection with Intermatic's advertising, displaying, offering for sale, sale or distribution of electric water heater timers except that paragraphs I.C., X., XI., and XII. also apply to any other electric appliance or device which is promoted, displayed, offered for sale or distributed directly or indirectly to consumers, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

I. *It is ordered,* That Intermatic cease and desist from representing, directly or by implication, that:

A. Use of Intermatic's water heater timers will result in substantial savings on hot water heating bills without significant reduction in the temperature or quantity of hot water used, except where the savings would be attributable to the consumer's use of the timer to take advantage of utilities' discount or time-of-day rates.

B. Significant cost savings from the use of the water heater timer are attributable to saving energy used by water heaters during periods when no hot water is being drawn off. This subparagraph does not prohibit respondent from making any representation that meets the requirements of subparagraph I.C., below.

C. Any energy or cost savings can be realized by any electric appliance or device unless Intermatic has a reasonable basis in valid scientific studies or tests from which to conclude that typical consumers, in the areas in which the representations are disseminated, will achieve those savings under expectable and usual consumer usage.

II. *It is further ordered,* That Intermatic make the following affirmative disclosures in any advertisement or promotional, labeling, or packaging material for its water heater timer:

A. That cost savings are accompanied by a decrease in the quantity and temperature of hot water available.

B. That dishwashers should be used during certain periods of the timer's cycle in order to operate properly.

The above affirmative disclosures shall be made clearly and conspicuously. The disclosure required in subparagraph II.A. shall be in close conjunction with and in type size at least as large as any reference to cost savings. In the case of packaging materials these disclosures need be made only once; the disclosure required in subparagraph II.A shall be on the most prominent face of each packaging material.

The above affirmative disclosure need not be made in any advertisement: (1) which is disseminated only in areas where some form of discount or time-of-day rates are offered by local utilities or where such rates are reasonably foreseeable; and (2) where no cost savings claim is made except a claim that the water heater timer provides savings by turning the water heater off during periods of higher rates.

The affirmative disclosure contained in subparagraph II.B. need not be made in advertising prepared by customers of respondent and for which respondent pays only part of the cost; *provided,* that the advertising appears as part of a multi-product advertisement the portion of which advertisement relating to the Intermatic water heater timer is no greater than eleven (11) square inches and the purpose of which is only to make the availability of the product at the retail outlet known.

III. *It is further ordered,* That Intermatic's instructions or directions for use of its water heater timer contain the following information in clear lay language:

A. The affirmative disclosures in paragraph II above. Type size shall be the same as (or larger than) that of the rest of the instructions or directions.

B. A statement that when the timer is off, the temperature of the water in the tank will decline. An explanation that if the consumer increases the amount of water drawn from the hot water tank as the temperature drops (such as by adjusting the hot/cold mix at a faucet) or uses any hot water during the "off" periods of the timer the temperature of available hot water will be decreased.

C. A method for using a dishwasher in order to have hot water available at the maximum temperature.

D. That the local electrical utility should be contacted to determine how to use timers on water heaters to avoid or minimize peak load demand problems for the utility.

E. A statement that in the event that the electrical utility serving the consumer introduces lower rates for "off peak" electrical consumption, the consumer should contact the utility to determine the "off-peak" periods so as to take advantage of lower rates.

IV. *It is further ordered,* That Intermatic immediately recall from all persons and entities that have engaged in the advertising, promotion, sale or distribution of the Intermatic water heater timer since January 1, 1977 (or request the disposal of) all advertising mats and promotional materials which contain a representation prohibited by this order or which omit a disclosure required by this order.

V. *It is further ordered,* That Intermatic prepare and distribute to all Intermatic customers who may reasonably be expected to have remaining stocks of the Intermatic water heater timer on hand, replacement packaging materials and instructions to conform with the terms of this order. Intermatic shall ask its customers to replace the packaging materials and instructions with the new ones provided, prior to making a further sale of the Intermatic water heater timer. In lieu of replacing the packaging materials Intermatic may provide its customers with self-adhesive labels to cover existing packaging materials.

VI. *It is further ordered,* That Intermatic distribute a copy of this order to each of its customers to which it has shipped five or more water heater timers at any time since January 1, 1977.

VII. *It is further ordered,* That Intermatic continue its present policy of refunding the purchase price and installation cost for the Intermatic water heater timer.

VIII. *It is further ordered,* That Intermatic prepare a point-of-sale display, in a form to be approved by authorized representatives of the FTC, which clearly and conspicuously (1) refers to the Intermatic "Little Gray Box" water heater timer; (2) contains the affirmative disclosures in paragraph II above; and (3) contains a statement of the refund policy required by paragraph VII above. Intermatic shall provide copies of the display, directly or through its distributors, to all retail stores which have sold the Intermatic water heater timer at any time since January 1, 1977, and request that the stores post the display for at least 30 days.

IX. *It is further ordered,* That respondent maintain complete business records relative to the manner and form of its compliance with this order. Respondent shall retain each record for at least three years, and shall retain substantiation and other documentation at least two years beyond the last dissemination of any representation contingent thereon under the provisions of this order. Upon reasonable notice, respondent shall make any and all the records available for inspection and photocopying by authorized representatives of the Federal Trade Commission.

X. *It is further ordered,* That respondent forthwith deliver a copy of this order to each operating division and affiliated business, to all present and future franchisees and licensees, and to all employees or agents now or hereafter engaged in the sale or offering for sale of respondents's products or in any aspect of the preparation, creation or placing of advertising on behalf of respondent; and that respondent secure from each such person a signed statement acknowledging receipt of this order. In the case of persons or entities not involved with respondent's water heater timers, this paragraph shall be satisfied by delivery of a statement including, verbatim, the order preamble and paragraph I.C., above.

XI. *It is further ordered,* That respondent notify the Commission at least thirty days prior to any proposed change in a corporate respondent in which the respondent is not a surviving entity, such as dissolution, assignment or sale resulting in the emergence of any successor corporation or corporations, or any other change in said corporations which may affect compliance obligations arising out of the order.

XII. *It is further ordered,* That respondent shall, within sixty days after service upon it of this order, file with the Commission a report setting forth in detail the manner and form in which it has complied with this order.

IN THE MATTER OF

HUK-A-POO SPORTSWEAR, INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2962. Complaint, April 25, 1979 — Decision, April 25, 1979

This consent order, among other things, requires two New York City wearing apparel manufacturers to cease establishing, maintaining or enforcing resale price agreements; suggesting retail prices or issuing price lists for a three-year period; pre-ticketing products with recommended retail prices; soliciting the identity of non-conformers and taking any adverse action against them. Additionally, respondents are required to reinstate customers who were terminated since January 1, 1974 for failing to maintain suggested prices; and keep records regarding reinstatement requests for five years.

Appearances

For the Commission: *Judith Braun* and *Sandra Bird.*

For the respondents: *Gilbert S. Edelson, Rosenman, Colin, Freund & Cohen,* New York City.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that the parties identified in the caption hereof, hereinafter sometimes referred to as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Huk-A-Poo Sportswear, Inc. and Pranx Fashions, Inc. are corporations organized, existing and doing business under and by virtue of the laws of the State of New York.

PAR. 2. Respondents are now, and have been engaged in the manufacture, sale and distribution of wearing apparel. In 1977 respondents had net sales in excess of $ 70,000,000.

PAR. 3. Respondents sell and distribute their products to retail dealers located throughout the United States who in turn resell respondents' products to the general public.

PAR. 4. In the course and conduct of their business as aforesaid, respondents cause and have caused apparel and related products to be shipped from the states in which they are manufactured or warehoused to purchasers in other states. Respondents maintain and at all times mentioned herein have maintained a substantial course of trade in or affecting commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended.

PAR. 5. For purposes of the complaint, the following definitions shall apply:

"Reseller" is defined as any person, firm or corporation which sells any product sold or distributed by any respondent.

"Prospective reseller" is defined as any person, firm or corporation which requests to purchase any product from any respondent.

"Resale price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula or margin of profit used by any reseller for pricing any product. Such term includes but is not limited to any suggested, established or customary resale price.

"Sale period" is defined as any break date, end of season or period for selling or advertising any product at a price other than the suggested, established or customary price.

PAR. 6. Except to the extent that competition has been hindered, frustrated, lessened and eliminated by the acts and practices alleged in this complaint, respondents have been and are in substantial competition with persons or firms engaged in the manufacture, distribution or sale of apparel and related products.

PAR. 7. Respondents, unilaterally or in combination, agreement or understanding with some resellers or with the cooperation or acquiescence of other resellers, have engaged in the following acts or practices, among others:

(a) establishing agreements, understandings, or arrangements with resellers or prospective resellers that such resellers or prospective resellers will maintain certain resale prices or sale periods;

(b) informing resellers or prospective resellers, by direct and indirect means, that respondents expect or require such resellers or prospective resellers to maintain or adhere to certain resale prices or sale periods;

(c) suggesting resale prices to resellers or prospective resellers or otherwise informing them of the resale prices respondents deem appropriate;

(d) entering agreements, understandings or arrangements with resellers or prospective resellers that such resellers or prospective resellers will not advertise any respondent's first-line quality products at resale prices other than those established, suggested or deemed appropriate by such respondent;

(e) entering agreements, understandings or arrangements with resellers or prospective resellers that such resellers or prospective resellers will not advertise any respondent's close-out or promotional products or second-line quality or irregular products as having been manufactured by such respondent;

(f) directing, soliciting or encouraging resellers, salespersons, employees or agents to cooperate and assist in identifying and reporting any reseller or prospective reseller who is engaged in any of the following activities:

(1) offering for sale or selling any product at a resale price other than that which any respondent has established, suggested or deemed appropriate.

(2) advertising any first-line quality product at a resale price other than that which any respondent has established, suggested or deemed appropriate.

(3) advertising any close-out or promotional product or second-line quality or irregular product as having been manufactured by any respondent.

(g) threatening to terminate, terminating, warning, intimidating and harassing resellers engaged in, or suspected of engaging in, any of the activities set forth in subparagraph (f) (1)-(3) above and using various forms of coercion and discipline, including but not limited to delaying order shipments, limiting the frequency of visits by salesmen and restricting the availability of products, against such resellers; or,

(h) refusing to deal with certain prospective resellers who may engage in any of the activities set forth in subparagraph (f) (1)-(3) above.

PAR. 8. The acts, practices and methods of competition engaged in, followed, pursued or adopted by respondents, as hereinabove alleged, have the capacity, tendency or the effect of:

(a) fixing, maintaining or stabilizing the resale prices for respondents' products;

(b) suppressing or eliminating competition between or among resellers of respondents' products;

(c) depriving resellers of their freedom to function as free and independent businessmen; and

(d) depriving consumers of the benefits of competition.

PAR. 9. The aforesaid acts, practices and methods of competition constitute unfair methods of competition and unfair acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the New York Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents, their attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondents Huk-A-Poo Sportswear, Inc. and Pranx Fashions, Inc. are corporations organized, existing and doing business under and by virtue of the laws of the State of New York, with their office and principal place of business located at 48 West 38th St., New York, New York.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

For purposes of this order, the following definitions shall apply:

"Reseller" is defined as any person, firm or corporation which sells any product sold or distributed by any respondent.

"Prospective reseller" is defined as any person, firm or corporation which requests to purchase any product from any respondent.

"Resale price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula or margin of profit used by any reseller for pricing any product. Such term includes but is not limited to any suggested, established or customary resale price.

"Sale period" is defined as any break date, end of season or period for selling or advertising any product at a price other than the suggested, established or customary price.

"Product" is defined as apparel or apparel accessories including but not limited to handbags, belts, gloves, scarves, hats, jewelry and footwear.

I

It is ordered, That each of the respondents Huk-A-Poo Sportswear, Inc. and Pranx Fashions, Inc., corporations, their successors and assigns, and each of the respondents' officers, agents, representatives and employees, directly or indirectly, or through any corporation, subsidiary, division or other device, in connection with the manufacture, offering for sale, sale, distribution or advertising of any product in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, shall forthwith cease and desist from:

1. Establishing, exacting assurances to comply with, continuing or enforcing any combination, agreement, understanding or arrangement to fix, establish, control, maintain or enforce, directly or indirectly, the price at which any product is to be resold or advertised by any reseller or prospective reseller.
2. Communicating, publishing, circulating, disseminating or providing by any means any resale price or sale period to any reseller or prospective reseller for a period of three (3) years from the date of service of this order; *provided, however,* that after said three (3) year period, a respondent shall not resume suggesting any resale price or sale period until it has mailed to all its open accounts a letter stating that no reseller is obligated to adhere to any suggested resale price or sale period and that suggested resale prices or sale periods are for informational purposes only.

Provided further, however, that after said three (3) year period, a respondent shall not suggest resale prices or sale periods unless it is clearly and conspicuously stated on those pages of any list, book, advertising or promotional material or other document where any suggested resale price or sale period appears:

THE [RESALE PRICES OR SALE PERIODS] QUOTED HEREIN ARE SUGGESTED ONLY. YOU ARE FREE TO DETERMINE YOUR OWN [RESALE PRICES OR SALE PERIODS].

Provided further, however, that after said three (3) year period, a respondent shall not suggest resale prices on any tag, ticket or comparable marking affixed or to be affixed to any product.

3. Requiring or coercing any reseller or prospective reseller to establish, maintain, issue, adopt or adhere to any resale price or sale period.

4. Requiring or soliciting any reseller, prospective reseller, person or firm, either directly or indirectly, to report any reseller, prospective reseller, person or firm that does not adhere to any resale price or sale period.

5. Communicating with any reseller or prospective reseller concerning its deviation or alleged deviation from any resale price or sale period.

6. Suggesting or requiring that any reseller or prospective reseller refrain from or discontinue advertising any product at a certain resale price.

7. Representing that any action may or will be taken against any reseller if it deviates from any resale price or sale period.

8. Threatening to withhold or withholding advertising allowances or any other assistance, payment, service or consideration from any reseller, or limiting or restricting the eligibility of any reseller to receive such benefits because said reseller advertises or sells any product at a certain resale price.

9. Making any payment or granting any other consideration or benefit to a reseller because another reseller has sold any product at a certain resale price.

10. Hindering or precluding the lawful use by any reseller of a brand name of any respondent in conjunction with the sale or advertising of any product at any price.

11. Refusing to sell to, terminating, suspending, delaying shipments to or taking or threatening any action against any reseller or prospective reseller because the reseller or prospective reseller has, or was alleged to have, sold or advertised any product at a certain resale price or because the reseller or prospective reseller may engage in any such activity in the future.

12. Attempting to secure any promise or assurance from any reseller or prospective reseller regarding the price at which such reseller or prospective reseller will or may advertise or sell any product; or requesting or requiring any reseller or prospective reseller to obtain approval from any respondent for any price at which such reseller or prospective reseller may or will advertise or sell any product.

II

It is further ordered, That respondents shall:

1. Within sixty (60) days after the date of service of this order, mail under separate cover a copy of either this order or the Federal Trade Commission's news release in this matter to every present reseller of Huk-A-Poo Sportswear, Inc. or Pranx Fashions, Inc. An affidavit of mailing shall be sworn to by an official of respondents verifying that said mailing was completed.

2. Mail a copy of either this order or the Federal Trade Commission's news release in this matter to any reseller that purchases any product from Huk-A-Poo Sportswear, Inc. or Pranx Fashions, Inc. within five (5) years after the date of service of this order. The mailing required by this paragraph shall occur within thirty (30) days after first purchase by said reseller.

3. Within thirty (30) days after the date of service of this order distribute a copy of this order to each of respondents' operating divisions and subsidiaries and to all officers, sales personnel, sales agents, sales representatives and advertising agencies retained by each respondent and secure from each entity or person a signed statement acknowledging receipt of said order.

4. Within sixty (60) days from the date of service of this order, mail or deliver, and obtain a signed receipt therefor, an offer of reinstatement, to every reseller who was terminated for failing to maintain a certain resale price or sale period by any respondent during the period from January 1, 1974 to the date of service of this order, unless the reseller does not meet the credit requirements applied by respondents in the retention of accounts, and reinstate any such reseller who requests reinstatement within thirty (30) days after receiving the offer.

5. Notify the Commission at least thirty (30) days prior to any proposed change in any respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation of or dissolution of subsidiaries or any other such change in the corporations which may affect compliance obligations arising out of the order.

6. For a period of five (5) years from the date of service of this order maintain complete business records which fully disclose the manner and form of respondents' compliance with the order, including but not limited to any records referring or relating in whole or in part to:

(a) any communication between any respondent and any reseller or prospective reseller relating to the price at which any reseller or prospective reseller is selling, proposes to sell, is advertising or proposes to advertise any product;

(b) the termination or suspension of any reseller for any reason;

(c) the refusal to deal with any prospective reseller for any reason, including the name and address of the prospective reseller; or

(d) any request for reinstatement pursuant to Part II Paragraph (4) of this order.

The records required by this paragraph shall be made available to Commission staff upon reasonable notice.

7. File with the Commission within sixty (60) days after service of this order a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

IN THE MATTER OF

RENAULT U.S.A., INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND MAGNUSON-MOSS WARRANTY — FEDERAL TRADE COMMISSION IMPROVEMENT ACTS

Docket C-2960. Complaint, April 26, 1979 — Decision, April 26, 1979

This consent order, among other things, requires an Englewood Cliffs, N.J. seller and distributor of automobiles to cease limiting the duration of implied warranties; make available to purchasers who had been issued incorrect written limited warranties all relief provided by applicable state law; and refrain from raising any defense relating to the limitation of implied warranties in law suits brought by such purchasers. Additionally, the firm is required to notify all purchasers who had received incorrect written limited warranties that they have an implied warranty on the drive train of their vehicle for as long as four years, depending on state law; and furnish them with an explanation of how implied warranties protect consumers. The firm is also required to advise their dealers of servicing obligations to purchasers who had been issued improper written limited warranties.

Appearances

For the Commission: *Michael E.K. Mpras* and *Jeffrey M. Parp.*

For the respondent: *Joseph C. Truncale,* Englewood Cliffs, N.J. and *Milton D. Andrews, Rivkin, Sherman & Levy,* Washington, D.C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, and of the Magnuson-Moss Warranty—Federal Trade Commission Improvement Act ("Warranty Act"), and by virtue of the authority vested in it by these Acts, the Federal Trade Commission having reason to believe that Renault U.S.A., Inc., a corporation, ("respondent") has violated the provisions of these Acts and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey with its office and principal place of business located at 100 Sylvan Ave., Englewood Cliffs, New Jersey.

PAR. 2. Respondent has been, and is now engaged in the distribution and sale of automobiles to the public.

PAR. 3. In the course and conduct of its business respondent is a supplier of consumer products distributed in commerce, as "supplier," "consumer product," and "commerce" are defined by Sections 101(4), 101(1) and 101(13) and (14) of the Warranty Act respectively. In connection with the distribution in commerce of its consumer products, manufactured subsequent to July 4, 1975, respondent offers a written warranty, as "written warranty" is defined by Section 101(6) of the Warranty Act and is therefore a warrantor, as "warrantor" is defined by Section 101(5) of the Warranty Act.

PAR. 4. In the course and conduct of its business, respondent has offered and continues to offer a written limited warranty covering the internal engine, internal transmission (manual or automatic) and internal differential parts of its new cars for a period of 24 months or 24,000 miles from the date of delivery or first use, whichever comes first.

PAR. 5. In connection with the respondent's offering of written warranties, respondent has incorrectly attempted to limit all implied warranties (with the exception of the emission control systems warranty) including the implied warranty of merchantability and the implied warranty of fitness for a particular use, arising under state law and available to purchasers of respondent's cars, to a period of 12 months or 12,000 miles from the date of delivery of the car or its first use. Therefore, respondent has limited all implied warranties with respect to the internal engine, internal transmission (manual or automatic) and internal differential parts to a period of 12 months or 12,000 miles from the date of delivery of the car or its first use.

PAR. 6. Respondent's limitation of the implied warranties as described in Paragraph Five of this complaint is a violation of Section 108 of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act and the Magnuson-Moss Warranty - Federal Trade Commission Improvement Act ("Warranty-Act"); and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Renault U.S.A., Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its office and principal place of business located at 100 Sylvan Ave., in the City of Englewood Cliffs, State of New Jersey.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

I. Definitions

For the purposes of this order the definitions of (1) the terms "written warranty" and "consumer product" as defined in Section 101 of the Warranty Act shall apply, and (2) "incorrect limitation" shall mean the attempted limitation of the duration of the implied warranties on the internal engine, internal transmission (manual or automatic) and internal differential parts to 12,000 miles or 12 months, whichever comes first, as set forth in Paragraph Five of the complaint.

II.

It is ordered, That respondent Renault U.S.A., Inc., a corporation, its successors and assigns, and its officers, representatives, agents and employees, directly or indirectly, through any corporation, subsidiary, division or any other device in connection with the advertising, offering for sale and sale of motor vehicles shall do the following:

A. Shall not limit the duration of the implied warranties with respect to any motor vehicle or part of such vehicle for a period which is shorter than the period of the express written warranty applicable to such motor vehicle or part.

B. For the period allowed by applicable state law:

1. Shall not raise any defenses pertaining to the limitation or modification of implied warranties as they relate to the internal engine, internal transmission and internal differential parts, in any case, suit or other proceeding brought against respondent by consumers who have purchased any of respondent's warranted motor vehicles manufactured after July 3, 1975 and were issued a written limited warranty stating the incorrect limitation.

2. Provide, in good faith, all consumers who have purchased any of respondent's warranted motor vehicles manufactured after July 3, 1975 and were issued a written limited warranty stating the incorrect limitation and which motor vehicles do not comply with all of the implied warranties as they relate to the internal engine, internal transmission and internal differential parts, with all relief available to them by applicable state laws.

C. Notify all consumers who have purchased any of respondent's warranted motor vehicles manufactured after July 3, 1975 and were issued a written limited warranty stating the incorrect limitation, by mailing to each such consumer the notice set forth in Appendix A of this complaint and order. In order to comply with this paragraph, respondent must ascertain who are registered under state law as the owners of such vehicles, and whose names and addresses are reasonably ascertainable through such state records by a commercial locator engaged by respondent.

D. Notify, by letter, all of its authorized Renault dealerships that respondent may be liable to all Renault owners who purchased Renault vehicles manufactured after July 3, 1975 and were issued a written limited warranty stating the incorrect limitation for breach of the implied warranties, including the implied warranty of merchantability and the implied warranty of fitness for a particular purpose for the period of time allowed by applicable state law. This notice shall, also, instruct the dealerships as to their servicing obligations, procedure for warranty claims by affected Renault owners and compensation of dealerships by respondent for work done pursuant to respondent's amended warranties and service manuals, and this order.

E. Notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any change in the corporation which may affect compliance obligations arising out of the order.

F. Deliver instructions, pursuant to this order, or a copy of this order, to all present and future personnel, agents and representatives of respondent, located in national or regional distribution offices, who review and approve warranty claims, and provide technical assistance regarding warranty claims, service and performance.

G. Maintain, for a period of three (3) years from the effective date of the order, complete business records of the manner and form of respondent's continuing compliance with all the terms and provisions of this order, to be furnished, upon request to the staff of the Federal Trade Commission during normal business hours and upon reasonable advance notice.

H. Shall within sixty (60) days after service upon it of this order, file with the Commission a report in writing, setting forth in detail the manner and form in which it has complied with this order.

Appendix A

Dear Renault Owner:

Following a review of our written Limited Warranty by the Federal Trade Commission, it was pointed out to us that we had made an error in part of our written Limited Warranty. We have voluntarily agreed with the FTC to write you this letter as part of a way to correct that error. FTC Dkt. C-2960, April 26, 1979.

When you bought your Renault car you also received a copy of our Limited Warranty. That warranty was for 12 months or 12,000 miles from the date of delivery or first use, whichever comes first, with additional coverage for 24 months or 24,000 miles on the drive train (which covers internal engine, internal transmission and internal differential parts). Included in that warranty, found in your warranty and maintenance guide, is a paragraph labeled "Implied Warranties Limitation" in which we incorrectly limited your implied warranties to 12 months or 12,000 miles on the drive train.

The Federal Warranty Law, the Magnuson-Moss Warranty Act, does not allow the implied warranties to run for a period shorter than the express written limited warranty. Because of our error, you now have implied warranties on the drive train of your car for as long as four years, depending on what your state law provides. Implied warranties are rights created by state law, not by Renault or any other company. All states have them and they are in addition to the protection you get from written warranties (like our Limited Warranty). The most common implied warranty is the warranty of merchantability. This means that we promise that the car you bought is fit for the ordinary uses of the car, which include safe, efficient driving.

Another implied warranty is the warranty of fitness for a particular purpose. If you bought your car relying on our advice or statements in our advertisements that it can be used for a special purpose, then this advice may create a warranty.

The above discussion refers only to *implied warranties. Renault reminds you that in no event is your written warranty on the drive train extended beyond 24 months or 24,000 miles.*

If you feel that your car has a defect that is covered by either of these implied warranties, please contact your dealer, or call us at (telephone number) (this is a toll-free number for you).

If you have sold your car, please tell the new owner about this, or tell us and we will write to him/her.

Sincerely,

RENAULT U.S.A., INC.
Customer Relations Department

IN THE MATTER OF

CAVANAGH COMMUNITIES CORPORATION, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9055. Complaint, Sept. 16, 1975 — Decision, May 3, 1979

This consent order, among other things, requires a Miami, Fla. land sales firm and eight wholly-owned subsidiaries to cease misrepresenting or failing to disclose the nature and purpose of promotional activities; the legal significance of signing a contract form; the monetary risks involved in the purchase of undeveloped land; and the advisability of consulting with a real estate specialist prior to purchase. Unavailability of utilities, sewage disposal, water, or other improvements must be set forth in contracts, and respondents are required to provide purchasers with a cooling-off period in which to cancel their dealings. The order also requires that purchasers be informed that certain subdivisions are located in designated flood areas and considerable expenditure would be required to make lots usable. Any sales representation concerning the availability of electricity, phone service, recreational facilities, and/or other improvements must be contractually guaranteed, and failure to fulfill such obligations in a timely manner would entitle purchasers to a refund of their full purchase price plus 7% interest. In addition, the order limits purchasers' liability in the event of default, and requires respondents to send previous buyers prescribed "truth" letters which contain information about investments, subdivision development, assessments, contractual rights, and possible tax benefits should purchasers default.

Appearances

For the Commission: *Jeffrey Tureck, Dayle Berke, D. McCarty Thornton* and *Pamela B. Stewart.*

For the respondents: *Philip F. Ziedman* and *Daryl A. Nickel, Brownstein, Zeidman, Schomer & Chase,* Washington, D.C.

COMPLAINT*

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Cavanagh Communities Corporation (formerly Cavanagh Leasing Corporation), a corporation, and its wholly-owned subsidiary corporations, Cape Cave Corporation, Cavanagh Marketing Corporation (formerly Cavanagh Land Sales Corporation), Cavad, Inc., Universal Properties, Inc., Wellington Orient, Inc., Miami Beach Vacations, Inc., Palm

* Reported as amended by Order Granting In Part And Remanding In Part Motion To Serve Supplemental Pleading dated January 27, 1976.

Beach Investment Properties, Inc., and Perdido Bay Management Corp., and their subsidiaries, and Joseph Klein and Arthur Meltzer, individually and as past or present officers and/or directors of Cavanagh Communities Corporation and one or more of said subsidiary corporations, hereinafter sometimes referred to as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating its charges in that respect as follows:

1. Respondent Cavanagh Communities Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 444 Brickell Ave., Miami, Florida.

2. Respondent Cavanagh Communities Corporation, from its aforementioned principal place of business, operates through, dominates and controls the acts and practices of its aforementioned subsidiaries, and their subsidiaries, and derives pecuniary and other benefits from the acts and practices of the said wholly-owned subsidiaries.

3. Respondent Cape Cave Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 444 Brickell Ave., Miami, Florida.

4. Respondents Cavanagh Marketing Corporation, Cavad, Inc., Wellington Orient, Inc., Miami Beach Vacations, Inc., Palm Beach Investment Properties, Inc., and Perdido Bay Management Corp., are corporations organized, existing and doing business under and by virtue of the laws of the State of Florida, with their principal offices and places business located at 444 Brickell Ave., Miami, Florida.

5. Respondent Universal Properties, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Ohio, with its principal office and place of business located at 444 Brickell Ave., Miami, Florida.

6. Respondents Joseph Klein and Arthur Meltzer are now and/or have been officers and directors of respondent Cavanagh Communities Corporation and several of the other corporate respondents. They formulate, direct and control, and for some time last past have formulated, directed and controlled, the acts and practices of such corporate respondents, including the acts and practices hereinafter set forth. Their address is 444 Brickell Ave., Miami, Florida.

7. Respondents Cavanagh Communities Corporation, Cape Cave Corporation, Cavanagh Marketing Corporation, Cavad, Inc., Universal Properties, Inc., and Wellington Orient, Inc., are now, and for

some time last past have been, engaged directly or through their wholly-owned subsidiaries in the business of acquiring undeveloped land, subdividing said land into lots, and advertising, offering for sale, and/or selling said lots to the public.

8. Respondents Palm Beach Investment Properties, Inc. and Perdido Bay Management Corp., are now, and for some time last past have been, engaged in the business of advertising, offering for sale, and sale to the public of lots owned by respondents or others.

9. Respondent Miami Beach Vacations, Inc. is now, and for some time last past has been, engaged in the publication, promotion, sale and distribution of room accommodation certificates ("vacation certificates") to consumers and businesses.

10. Among the subdivisions in which lots have been and/or are being offered for sale by respondents are the subdivisions known as Rotonda West, Rotonda Shores, Rotonda Heights, Rotonda Lakes, Rotonda Meadows, Rotonda Springs, Rotonda Sands, Rotonda Villas, Paradise Hills, Enterprise Heights-Timber Ridge, Palm Beach Heights, Palm Beach Country Estates, and Perdido Bay Country Club Estates, all located in the State of Florida, and Twin Lakes Country Club & Estates, located in the State of Arizona.

11. Respondents usually sell the lots in their subdivisions to purchasers who have not seen the property by means of standard form contracts, generally titled "Agreement for Deed," hereinafter referred to in this complaint as a "contract," whereby the purchaser pays monthly installments over a term of several years. According to the provisions of the contract, title to and possession of the lot remain in the respondents until all payments are made, at which time title to the lot is to pass to the purchaser. As to most of their subdivisions, respondents agree in the contract to make certain improvements of benefit to the lot, said improvements to be completed before title passes. Purchasers do not, during the term of the contract, enjoy any rights of enjoyment of the lot. The contract provides that the purchaser pays interest to the respondents during the contract term on the unpaid balance owing under the contract.

12. In the course and conduct of their aforesaid business respondents now cause, and for some time last past have caused, their promotional materials, contracts and various business papers to be transmitted through the U.S. mail and other interstate instrumentalities from their places of business in Arizona, Florida and other states to their agents, representatives, employees, customers and prospective customers in various other States and Territories of the United States and the District of Columbia and foreign nations, and now maintain and operate, and for some time last past have

maintained and operated, places of business and have made substantial sales to purchasers in the various other States of the United States and the District of Columbia and in foreign nations, and maintain, and at all times mentioned herein have maintained, a substantial course of trade in said land in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

13. In the course and conduct of their aforesaid business, and at all times mentioned herein, respondents have been, and now are, in substantial competition, in or affecting commerce, with corporations, firms and individuals in the sale of land.

14. In the course and conduct of the aforesaid business, respondents disseminate advertisements through television and radio broadcasts and in various publications of general circulation, distribute promotional materials through the mail and in person to members of the public, and make sales presentatons by means of oral and written statements, slides and movies. By and through such means, respondents have made and are making various statements and representations, directly or by implication, concerning the good reputation, financial security, and integrity of Cavanagh Communities Corporation and its predecessor corporation.

15. By and through the use of such statements and representations, respondent Cavanagh Communities Corporation has permitted and participated in the use of its name and its alleged good reputation, financial security, and integrity for the purpose of selling its subsidiaries' land and deriving pecuniary benefits therefrom.

I

16. In the further course and conduct of their aforesaid business, respondents disseminate advertisements through television and radio broadcasts and in various publications of general circulation, distribute promotional materials through the mails and in person to members of the public, and make sales presentations by means of oral and written statements, movies and slides. By and through such means, respondents have made and are making various statements and representations concerning the supply of and demand for land; the liquidity or marketability of land; land prices and values; land as an investment; inflation; the stock market, banks and insurance; population growth and movement; the location of industrial, commercial and recreational facilities; the suitability of lots in respondents' properties for investments or homesites; the present and future development of respondents' subdivisions; the financial integrity and reputation of respondents as a community developer; the well-known personalities who live in or near subdivisions in

which respondents are selling land; and the various options or financial protections afforded purchasers of respondents' land, including the repurchase or resale by respondents of lots acquired by purchasers from respondents.

17. By and through the statements and representations alleged in Paragraph 16 above, respondents have represented and are representing, directly or by implication, that the lots which respondents are offering for sale are, at the price at which respondents are offering them for sale, investments which will provide significant financial return to the purchasers, and that there are few or no financial risks involved in the purchase of said lots at said price.

18. In truth and in fact, in a significant number of instances, the lots which respondents are offering for sale, at the price at which respondents are offering them for sale, are not investments which will provide significant financial return to purchasers, and involve substantial financial risk to purchasers. Therefore, the acts and practices alleged in Paragraph 17 above are deceptive.

II

19. In the further course and conduct of their aforesaid business, respondents have offered and are offering lots for sale without disclosing to prospective purchasers that the lots being offered are, at the price at which respondents are offering them, a risky investment in that, *inter alia,* the future value of the lots being offered is uncertain and the purchaser probably will be unable to sell his lot, or his interest in it under contract, at or above the purchase price, if at all. Respondents therefore have failed to disclose material facts which, if known to certain consumers, would be likely to affect their consideration of whether to purchase a lot from respondents. Such failure to disclose is a deceptive or unfair act or practice.

III

20. In the further course and conduct of the aforesaid business, respondents have made and are making various oral and written statements and representations to prospective purchasers and purchasers concerning repurchase or resale by respondents of lots acquired by purchasers from respondents.

21. By and through the statements and representations alleged in Paragraph 20 above, respondents have represented and are representing, directly or by implication, that they will either buy back from or resell for purchasers lots acquired from respondents at or above the price paid for said lots by the purchasers.

22. In truth and in fact, respondents do not buy back from or resell for purchasers lots acquired from respondents. Therefore, the act or practice alleged in Paragraph 21 above is unfair or deceptive.

IV

23. In the further course and conduct of the aforesaid business, and after a purchaser has signed a contract, respondents have made and are making various statements and representations to such purchasers through oral and written statements, concerning the current value of lots which have previously been purchased from respondents.

24. By and through the representations alleged in Paragraph 23 above, respondents have represented and are representing, directly or by implication, that such purchasers' lots are currently worth significantly more than the price paid for such lots by the purchasers.

25. In truth and in fact, after lots are purchased from respondents they generally are not worth significantly more than the price paid by the purchaser. Therefore, the acts and practices alleged in Paragraph 24 are deceptive or unfair.

V

26. In the further course and conduct of their aforesaid business, respondents have made and are making statements and representations in promotional materials and in sales presentations by means of oral and written statements, films and slides, concerning the reputation and experience of respondents as community developers.

27. By and through the statements and representations alleged in Paragraph 26 above, respondents have represented and are representing, directly or by implication, that:

a) Respondents are experienced community developers.

b) Respondents have developed and are developing new communities throughout the United States.

28. In truth and in fact:

a) At the time the first such representations were made respondents were not experienced community developers.

b) Respondents have not developed and are not developing new communities throughout the United States.

Therefore, the statements and representations alleged in Paragraph 27 above are deceptive or unfair.

VI

29. Respondents, in the further course and conduct of their aforesaid business, have offered and are offering for sale lots in subdivisions having similar names. Said subdivisions are often referred to collectively or conjunctively.

30. The practices alleged in Paragraph 29 above have the capacity and tendency to lead significant numbers of consumers into the belief that the recreational facilities, improvements, utilities, and amenities to be provided for one such subdivision are the same as those for one or more of the other subdivisions, or that the aforesaid subdivisions are a single subdivision to which all of respondents' representations concerning recreational facilities, improvements, utilities and amenities are applicable.

31. In truth and in fact, all of the aforesaid subdivisions are not going to be provided with identical recreational facilities, improvements, utilities and amenities, Therefore, the practices alleged in Paragraph 29 above are deceptive or unfair.

VII

32. In the further course and conduct of the aforesaid business, respondents have made and are making various statements and representations to members of the public, by means of advertisements in various publications of general circulation, promotional materials, TV and radio broadcasts, telephone calls, and sales presentations involving oral statements, written statements, movies and slides, concerning the past, present, and future development of the Rotonda subdivisions; including the various recreational facilities, improvements, utilities and amenities to be provided in and for Rotonda West and the other Rotonda subdivisions; the progress being made toward their completion; the various construction projects which have been planned and/or begun in the Rotonda subdivisions and the cost of acquiring a lot to which the various recreational facilities, improvements and utilities are or will be available.

33. By and through the statements and representations alleged in Paragraph 32 above concerning the Rotonda subdivisions, respondents have represented and are representing, directly or by implication, that:

a) Certain recreational facilities, improvements, utilities and amenities, including but not limited to a multi-million dollar clubhouse, totally underground utilities, concrete curbs and gutters, sidewalks, and a park and business complex, will be provided in Rotonda West and/or the other Rotonda subdivisions.

b) Certain recreational facilities, buildings, and amenities, including but not limited to a golf course, multi-family residential buildings, and a strip shopping center, are planned for completion by dates certain.

c) Certain recreational facilities and buildings, including but not limited to a clubhouse and a multi-family residental development, are under construction.

d) Certain buildings, including but not limited to a hotel or motel and a townhouse development, are planned for the immediate future.

e) A stated member of miles of certain improvements, including but not limited to curbs and gutters and roads, have been completed.

34. In truth and in fact:

a) The recreational facilities, improvements, utilities and amenities referred to in subparagraph 33(a) above are not part of respondents' express contractual obligations to purchasers. In addition, these recreational facilities, improvements, utilities and amenities:

(i) Were not, at the time the representations referred to in subparagraph 33(a) were made, part of respondents' development plans for any of the Rotonda subdivisions and the Rotonda community, or were part of respondents' development plans for only a single segment of Rotonda West; and/or

(ii) Are not presently part of respondents' development plans for any of the Rotonda subdivisions and the Rotonda community, or are part of respondents' development plans for only a single segment of Rotonda West.

b) The recreational facilities, buildings, and amenities referred to in subparagraph 33(b) above were not completed by the dates represented and still have not been completed.

c) The recreational facilities and buildings referred to in subparagraph 33(c) above were not under construction at the time the representations were made and are still not under construction.

d) The buildings referred to in subparagraph 33(d) above were never constructed.

e) Substantially fewer miles of the improvements referred to in subparagraph 33(e) above had actually been completed at the time the representations were made.

Therefore, the acts and practices alleged in Paragraph 33 above are deceptive or unfair.

VIII

35. By and through the statements and representations alleged in Paragraph 32 above, respondents have further represented and are representing, directly or by implication, that all lots in the Rotonda subdivisions which will be served by a central sewerage system when required by population density will be able to use septic tanks prior to that time.

36. In truth and in fact, in many cases where it is respondents' contractual obligation to provide a central sewerage system to a lot when required by population density, no reasonable alternate means of sewage disposal is or will be available prior to that time.

Therefore, the acts and practices alleged in Paragraph 35 above are deceptive or unfair.

IX

37. By and through the statements and representations alleged in Paragraph 32 above, respondents have further represented and are representing, directly or by implication, that Don Pedro Island will be reserved as a private resort island for the exclusive use of purchasers of lots in the Rotonda subdivisions and their guests.

38. In truth and in fact, respondents have no express contractual obligations which require them to reserve Don Pedro Island as a private resort island for the exclusive use of Rotonda purchasers and their guests; in addition, respondents have permitted and/or plan to permit others to use Don Pedro Island. Therefore, the acts and practices alleged in Paragraph 37 above are deceptive or unfair.

X

39. In the further course and conduct of their aforesaid business, respondents have made and are making statements and representations in promotional materials and in sales presentations by means of oral and written statements, films and slides, concerning the past, present and future development of Twin Lakes Country Club and Estates and the future development of Paradise Hills, Palm Beach Heights, and Perdido Bay Country Club Estates.

40. By and through the statements and representations alleged in Paragraph 39 above, respondents have represented and/or are representing, directly or by implication, that in Twin Lakes Country Club & Estates:

a) Certain utilities, including but not limited to water and gas lines, are presently available to many lots.

b) Electricity will be made available to each lot for only a nominal hook-up charge.

c) Certain recreational facilities and amenities, including but not limited to lakes, a restaurant, and an 18 hole golf course, have been completed and are in use or will soon be made available.

d) Respondents will maintain all roads.

41. In truth and in fact, in Twin Lakes Country Club and Estates:

a) The utilities referred to in subparagraph 40(a) above were not available to many lots at the time the alleged representations were made, and are not presently available.

b) Electricity will be made available to many lots only upon the payment to the local utility company of a sizable line extension fee.

c) The recreational facilities and amenities referred to in subparagraph 40(c) above either have never been made available or were made available for only a short time and then closed down by respondents.

d) Respondents have not adequately maintained the roads.

Therefore, the acts and practices alleged in Paragraph 40 above are deceptive or unfair.

XI

42. By and through the statements and representations alleged in Paragraph 39 above, respondents have further represented and are representing, directly or by implication, that:

a) Paradise Hills would be developed at least to the extent of lots being made accessible by conventional means of transportation.

b) Palm Beach Heights would be a fully developed suburban community, with paved roads, recreational facilities, and other improvements and amenities.

c) The canals in Palm Beach Heights will be navigable when completed, and many lots therein will have access by boat to the Atlantic Ocean or other open water.

d) Many lots in Perdido Bay Country Club Estates would be completely developed within one or two years from the date of purchase.

43. In truth and in fact:

a) It is not part of respondents' express contractual obligations, nor is it part of respondents' land development program, to develop Paradise Hills in any manner whatsoever.

b) The contractual obligations and development plans for Palm Beach Heights are limited to dirt roads and drainage.

c) There are no contractual obligations or development plans to make the canals in Palm Beach Heights navigable or to provide access by boat to the Atlantic Ocean or other open water.

d) It is not part of the land development plans for Perdido Bay Country Club Estates to develop the lots therein prior to the date for completion of improvements stated in the purchaser's contract.

Therefore, the acts and practices alleged in Paragraph 42 above are deceptive or unfair.

XII

44. In conjunction with the statements and representations alleged in Paragraphs 32 and 39 above regarding improvements and utilities, and statements and representations in sales presentations regarding the cost of a lot, respondents have failed and are failing to clearly and conspicuously disclose that, in order to purchase a lot and render it suitable for use, the purchaser must incur substantial additional expenses which are not included in the purchase price. The necessity of incurring such expenses is a material fact, knowledge of which would be likely to affect the decision of certain consumers as to whether to sign a contract for the purchase of respondents' land.

45. Therefore, the failure to clearly and conspicuously disclose the aforesaid substantial additional expenses in conjunction with the statements and representations alleged in Paragraph 44 above is a deceptive or unfair act or practice.

XIII

46. In the further course and conduct of their business, respondents have set up Conservation Associations in many of their subdivisions. These Associations, each of which is comprised of all owners of lots in one subdivision (including those undeeded purchasers still paying for lots under the terms of their contracts), have the right by a vote of the members to assess their members for the upkeep of and any capital improvements to the common properties in the subdivision. Until such time as 75% of the total number of lots in the subdivision are conveyed of record by respondents, respondents shall have all of the voting rights in that subdivision's Conservation Association.

47. Respondents fail to clearly and conspicuously disclose to potential purchasers the existence of the Conservation Associations in the subdivisions where applicable, that these Associations have the right to assess all property owners to maintain the common properties in the subdivision, and that respondents will be the sole

voting member of the association for the foreseeable future. Each of these facts is a material fact, knowledge of which would be likely to affect the decision of certain consumers as to whether to purchase a lot from respondents. Such failure to disclose is a deceptive or unfair act or practice.

XIV

48. In the further course and conduct of their business, respondents have made and are making oral statements to many purchasers of single family residential lots concerning the exchange of such lots for more expensive multiple family residential lots.

49. By and through the statements and representations alleged in Paragraph 48 above, respondents have represented and are representing, directly or by implication, that in the event the purchasers exchange their single family residential lots for more expensive multiple family residential lots, respondents will plan and construct, at the purchasers' expense, multiple family residences, and will act as the rental agent for such residences when completed.

50. In truth and in fact, respondents failed to construct such multiple family residences for purchasers who made the exchange to multiple family residential lots. Therefore, the acts and practices alleged in Paragraph 49 above are deceptive or unfair.

XV

51. In the further course and conduct of their aforesaid business, respondents have made and are making statements and representations in advertisements in publications of general circulation, promotional materials, and sales presentations by means of oral and written statements, films and slides, concerning the accessibility from the Rotonda subdivisions and certain lots therein to the Gulf of Mexico and the navigability and other uses of canals in the Rotonda subdivisions.

52. By and through the statements and representations alleged in Paragraph 51 above, respondents have represented and are representing, directly or by implication, that in the Rotonda subdivisions:

(a) The Gulf of Mexico is accessible by boat from marinas and from lots fronting on canals;

(b) All canals will be suitable for recreational uses including but not limited to boating and water skiing.

53. In truth and in fact:

(a) The Gulf of Mexico is not accessible by boat from marinas and lots fronting on canals in the Rotonda subdivisions;

(b) Many canals in the Rotonda subdivisions are suitable for recreational uses only to a limited extent.

Therefore, the acts and practices alleged in Paragraph 52 above are deceptive or unfair.

XVI

54. In the further course and conduct of their aforesaid business, respondents have made and are making various statements and representations to members of the public, by means of advertisements in various publications of general circulation, promotional materials, TV and radio broadcasts, telephone calls, and sales presentations involving oral and written statements, films and slides, concerning Ed McMahon, a well-known television personality, and his relationship with respondents.

55. By and through the statements and representations alleged in Paragraph 54 above, respondents have represented and are representing, directly or by implication, that:

a) Ed McMahon takes an active part in the day-to-day operation of respondent Cavanagh Communities Corporation's business.

b) Ed McMahon purchased real estate in Rotonda because he believed real estate in Rotonda was a good investment.

56. In truth and in fact:

a) Ed McMahon did not take an active part in the day-to-day operation of respondent Cavanagh Communities Corporation's business during the time he was employed by Cavanagh.

b) At the time the representation alleged in subparagraph 55(b) was first made, Ed McMahon did not own, and had not contracted to acquire, real estate in Rotonda.

Therefore, the acts and practices alleged in Paragraph 55 above are deceptive or unfair.

XVII

57. In the further course and conduct of their aforesaid business, respondents have made and are making statements in promotional materials concerning the participation of General Electric Co. in the planning and development of Rotonda West.

58. By and through the statements and representations alleged in Paragraph 57 above, respondents have represented, directly or by implication, that General Electric Co. played a major role in the planning, design and development of Rotonda West.

59. In truth and in fact, General Electric Co. did not play a major role and does not now play a major role in the planning, design and development of Rotonda West. Therefore, the acts and practices alleged in Paragraph 58 above are deceptive or unfair.

XVIII

60. In the further course and conduct of their aforesaid business, respondents have made statements and representations in promotional materials and in sales presentations by means of oral and written statements, films and slides concerning the limited size of the Rotonda community.

61. By and through the statements and representations alleged in Paragraph 60 above, respondents have represented that the Rotonda community will consist of only Rotonda West, or of only Rotonda West, Rotonda Heights, and Rotonda Lakes, and that the lots therein will therefore have great value.

62. In truth and in fact, the Rotonda community consists of Rotonda West, Rotonda Heights, Rotonda Lakes, and five other subdivisions. Therefore, the acts and practices alleged in Paragraph 61 above are deceptive or unfair.

XIX

63. In the further course and conduct of their aforesaid business, respondents have made and are making statements and representations in promotional materials and in sales presentations through oral and written statements, slides and films, concerning the population growth, present population, and population projections for various cities, counties, and states in which or in the vicinity of which their subdivisions are located.

64. By and through the statements and representations alleged in Paragraph 63 above, respondents have represented and are representing, directly or by implication, that their subdivisions are located in areas of unusually high population growth.

65. In truth and in fact, some of respondents' subdivisions are not located in areas of unusually high population growth. Therefore, the acts and practices alleged in Paragraph 64 above are deceptive and unfair.

XX

66. In the further course and conduct of their aforesaid business, respondents have offered and are offering lots for sale in certain subdivisions without clearly and conspicuously disclosing to prospec-

tive purchasers that the area comprising the subdivisions has been designated as a flood hazard area by the Federal Insurance Administration of the Department of Housing and Urban Development, and that such designation carries legal requirements and consequences which may significantly affect the use of and increase the costs of using the lots as homesites. Said designation and the legal consequences thereof are material facts, knowledge of which would be likely to affect the decision of certain consumers as to whether to purchase such lots. Therefore, the failure to disclose the aforementioned facts is a deceptive or unfair act or practice.

XXI

67. In the further course and conduct of their aforesaid business, respondents have offered certain residential lots for sale to prospective purchasers without clearly and conspicuously disclosing that such lots are located adjacent to or in the vicinity of railroad tracks which have been and are being used to carry trains. The aforementioned facts are material facts, knowledge of which would be likely to affect the decision of certain consumers as to whether to purchase such lots. Therefore, the failure to disclose the aforementioned facts is a deceptive or unfair act or practice.

XXII

68. In the further course and conduct of their aforesaid business, respondents have failed to clearly and conspicuously disclose to prospective purchasers and purchasers that certain previously disclosed plans for the development of their subdivisions and/or the recreational facilities, improvements, utilities, or amenities, therein, have been materially altered or that certain recreational facilities and amenities which were previously available for use or in operation have been subsequently closed or are no longer operational. The above facts are material facts, knowledge of which would be likely to affect the decision of certain prospective purchasers as to whether to purchase a lot from respondents, and of certain purchasers as to whether to continue to make their monthly payments, or, if applicable, whether to cancel their contracts and receive refunds in accordance with the refund privilege stated in their contracts. Therefore, such failure to disclose the aforementioned facts is a deceptive or unfair act or practice.

XXIII

69. In the further course and conduct of their aforesaid business,

respondents have failed to clearly and conspicuously disclose to consumers that as a condition to receiving free or low cost goods or services from respondents, or to use a vacation certificate issued by respondents and/or distributed to the public by respondents, the consumers will be required to attend a land sales presentation. The above-mentioned facts are material facts, knowledge of which would be likely to affect the decision of certain consumers as to whether to accept free or low cost goods and services from respondents or use vacation certificate issued or distributed to the public by respondents. Therefore, such failure to disclose is a deceptive or unfair act or practice.

XXIV

70. In the further course and conduct of their aforesaid business, respondents have made and are making various statements and representations in sales presentations concerning the import or significance of signing a contract for the purchase of respondents' land.

71. By and through the statements alleged in Paragraph 70 above, respondents have represented and are representing, directly or by implication, that by signing a contract, the purchaser is not entering into a binding obligation to purchase land.

72. In truth and in fact, a person signing a contract has thereupon entered into a binding obligation to purchase land. Therefore, the act or practice alleged in Paragraph 71 above is deceptive or unfair.

XXV

73. In the further course and conduct of the aforesaid business, respondents have made and are making various statements and representations in promotional materials and in sales presentations by means of oral and written statements, slides and movies, concerning a purchaser's right after signing a contract to rescind and obtain a full refund of all monies paid thereunder.

74. By and through the statements and representations alleged in Paragraph 73 above, respondents have represented, and are representing, directly or by implication, that in the event a purchaser completes a tour of the subdivision in which his or her lot is located within the required time period and immediately thereafter requests a refund, the purchaser will get a refund without difficulty.

75. In truth and in fact:

a) In many cases, respondents use high pressure tactics in order to induce purchasers who request refunds after the company-guided tour of the subdivision to change their minds. In other cases, respondents refuse to provide purchasers, within a reasonable period of time, with the form they are required to sign at the subdivision in order to obtain a refund.

b) In many cases, respondents do not send refunds to purchasers who are so entitled until the expiration of an unreasonable period of time.

Therefore, the acts and practices alleged in Paragraph 74 above are deceptive or unfair.

XXVI

76. In the further course and conduct of their aforesaid business, respondents have made and are making statements in promotional materials and orally in sales presentations concerning the price and location of the lots they are offering for sale and will offer for sale.

77. By and through the statements alleged in Paragraph 76 above respondents have represented and are representing, directly or by implication, that prospective purchasers must purchase a lot immediately to insure that the price will not increase and that the location they desire will be available.

78. In truth and in fact, most prospective purchasers do not have to purchase immediately to insure that prices will not increase or that desired locations will be available. Therefore, the acts and practices alleged in Paragraph 77 above are deceptive or unfair.

XXVII

79. In the further course and conduct of their aforesaid business respondents, in obtaining a purchaser's signature on a contract, have presented and are presenting purchasers with a contract, one or more property reports required to be provided to the purchaser by state and/or federal law, and in some instances additional lengthy or detailed documents. These documents contain information and provisions likely to affect the decision of certain consumers as to whether to sign a contract for the purchase of respondents' land.

80. Respondents have made and are making available the aforesaid documents at sales presentations or other gatherings sponsored by respondents in circumstances where it is likely that many purchasers will not read such documents because they are insufficiently aware of their utility or significance, or it is likely that many purchasers will not have the opportunity to read such

documents carefully, completely or with full comprehension of their meaning and import. The soliciting or obtaining under such circumstances of a purchaser's signature on a contract to purchase respondents' land, involving a substantial financial commitment by the purchaser, is a deceptive or unfair act or practice.

XXVIII

81. In the further course and conduct of the aforesaid business, respondents have utilized and are utilizing a contract the provisions of which cannot be understood by many consumers or cannot be evaluated by many consumers to determine if they are fair or reasonable. Respondents have made and are making available the contract to purchasers, and solicit and obtain signatures to the contract from purchasers, in circumstances where the purchaser has not had the opportunity to seek assistance or counsel in understanding the provisions or making the aforesaid determination.

82. The soliciting or obtaining of a purchaser's signature on a contract to purchase respondents' land, involving a substantial financial commitment by the purchaser, where the purchaser has not had opportunity to seek assistance or counsel for the purposes referred to in Paragraph 81 above, is an unfair act or practice.

XXIX

83. Respondents, in the further course and conduct of their aforesaid business, have utilized and are utilizing standard form contracts for the sale of lots to purchasers.

84. The aforesaid contracts contain a provision under which purchasers are entitled, at their option, to a refund of all payments or an exchange of property, if respondents fail to meet their obligations under the contracts. No requirement is imposed upon respondents by the aforesaid contract to inform purchasers that respondents have so failed to meet their obligations.

85. The absence of the aforesaid requirement to inform purchasers renders the use by respondents of the aforesaid contract provision an unfair act or practice because many purchasers, in the context of an interstate land sales transaction, are likely to remain unaware indefinitely of respondents' failure to meet their contractual obligations, and will therefore fail to seek the legal redress to which they may be entitled.

XXX

86. The aforesaid contracts also contain a provision that no oral

or implied representations have been made as an inducement to enter into the contract other than those expressly contained in the contract, or that no agreements, stipulations, representations, warranties, promises or understandings not expressly set forth in the contract have been made.

87. The use by respondents of the aforesaid provisions is an unfair or deceptive act or practice because respondents make representations, through advertisements in publications of general circulation, in promotional materials, and in sales presentations by means of oral statements, slides and movies, which differ in material respects from the obligations of respondents or purchasers under said contracts.

XXXI

88. The aforesaid contracts also contain a declaration by the purchaser that the purchaser has had an opportunity to examine any property reports or offering statements required to be made available to prospective purchasers by state or federal law, and that the purchaser understands that he has the right to cancel the contract within a time period which is therein stated.

89. The use by respondents of the aforesaid declaration is an unfair or deceptive act or practice because respondents frequently fail to give the purchaser the property report or offering statement prior to the signing by the purchaser of the contract, or frequently make available the property report or offering statement in circumstances where it is likely that many purchasers will not read such documents because they are insufficiently aware of their utility or significance, or it is likely that many purchasers will not read such documents carefully, completely or with full comprehension of their meaning and import.

XXXII

90. The aforesaid contracts also generally provide that upon a failure of the purchaser to pay any installment due under the contract, the seller shall be entitled to retain all sums previously paid thereunder by the purchaser as liquidated damages.

91. The use by respondents of the aforesaid provision is an unfair act or practice because the sums retained by the respondents are not calculated to bear any relation to the actual damages, if any, sustained by respondents by reason of the purchaser's default.

XXXIII

92. The aforesaid contracts also contain a refund provision according to the terms of which purchasers must personally complete a company-guided tour of the subdivision in which their lots are located within a specified period of time in order to obtain a refund of all moneys paid under their contracts. Many of the lots sold by respondents are physically inaccessible within the time period in which the purchaser has to make the tour, and thus purchasers completing this tour generally will not be able to see their lots. In addition, during and/or after the tour of the subdivision the purchasers generally will be subjected to attempts to sell them additional and/or more expensive land.

93. The use by respondents of the aforesaid provision is an unfair act or practice because it requires purchasers to incur the expense of traveling to the subdivisions in which their lots are located, and because it requires purchasers to be subjected to additional sales attempts, without significantly adding to purchasers' ability to make an informed judgment as to whether to retain their land.

XXXIV

94. Many of the aforesaid contracts for the purchase of a lot in one or more of the Rotonda subdivisions also contain provisions regarding respondents' obligations in the event neither central sewerage facilities nor septic tanks are available when the purchaser is ready to build on his lot. These contracts state that if central sewerage facilities are unavailable and a septic tank permit cannot be obtained, the purchaser and respondents will try to agree upon an exchange to a lot which does have sewage facilities. Should such an agreement not be reached, some of the aforesaid contracts contain no further relief for the purchaser; others provide that respondents will give the purchaser a refund of all payments without interest.

95. By and through the use of the contract provisions described in Paragraph 90 above, respondents have sold and are selling homesite lots which may not have any reasonable means of sewage disposal while at the same time limiting the remedies purchasers may seek against respondents in the event said lots in fact have no reasonable means of sewage disposal to remedies that do not adequately protect such purchasers. Therefore, the use by respondents of the aforesaid provisions is unfair or deceptive.

XXXIV-A

95a. In the further course and conduct of their aforementioned business, respondents have made and are making various statements and representations to purchasers by means of oral and written statements concerning the Federal Trade Commission's proceedings against Cavanagh Communities Corporation, *et al.* under Dkt. 9055, including but not limited to statements and representations characterizing the complaint allegations and describing their applicability to the Rotonda subdivisions.

95b. By and through the statements and representations alleged in Paragraph 95a above, respondents, directly or by implication, have misrepresented and are misrepresenting the contents of the aforementioned complaint, including but not limited to misrepresenting allegations regarding the use or value of lots in respondents' subdivisions as investments and homesites, the applicability of the various complaint allegations to the Rotonda subdivisions, and the nature of the allegations which do pertain to Rotonda. The making of such misrepresentations is a deceptive or unfair act or practice.

XXXIV-B

95c. In the further course and conduct of their aforementioned business, respondents have made and are making various statements and representations to purchasers by means of oral and written statements concerning the improvements made at Rotonda.

95d. By and through the statements and representations alleged in Paragraph 95c above, respondents have represented and are representing, directly or by implication, that respondents recently have made substantial improvements at Rotonda.

95e. In truth and in fact, there has been little or no recent development at Rotonda by respondents. Therefore, the acts and practices alleged in Paragraph 95d above are deceptive or unfair.

XXXV

96. In the further course and conduct of the aforesaid business, respondents as aforesaid have induced and are inducing members of the public to pay to them in advance of title or the obtaining of any rights of enjoyment or possession, substantial sums of money towards the purchase of lots in Rotonda West, Rotonda Shores, Rotonda Heights, Rotonda Lakes, Rotonda Meadows, Rotonda Springs, Rotonda Sands, Rotonda Villas, Paradise Hills, Palm Beach Heights, and Twin Lakes Country Club and Estates, which are of little value to purchasers as investments and little use as homesites. Such purchasers have paid and are paying such money towards the purchase of lots in reliance upon the aforementioned unfair and

deceptive statements, representations and practices. Respondents have received and are receiving the said sums and have failed to offer to refund or refused to refund such money to purchasers.

97. The use by respondents of the aforesaid practice and their continued retention of the sums, as aforesaid, is an unfair act or practice.

XXXVI

98. In the course and conduct of the aforesaid business, respondents as aforesaid, have engaged and are engaging in an unfair practice by utilizing in their standard form contracts a provision whereby defaulting purchasers forfeit all payments previously made to respondents under the contract. Respondents have received and are receiving the said payments and have failed to offer to refund or refused to refund to defaulting purchasers all payments in excess of respondents' reasonable damages caused by the purchaser's default.

99. The use by the respondents of the aforesaid contract provision and their continued retention of payments in excess of reasonable damages, as aforesaid, is an unfair act or practice.

XXXVII

100. Respondents have as aforesaid (i) induced and are inducing members of the public through unfair and deceptive acts and practices to pay to respondents substantial sums of money towards the purchase of lots in certain of respondents' subdivisions, and (ii) have continued to retain substantial sums in excess of their reasonable damages as a result, as aforesaid, of the unfair forfeiture provision in their contracts.

101. The effect of using the aforesaid acts and practices to secure and retain substantial sums of money is or may be to substantially hinder, lessen, restrain or prevent competition between respondent and the aforesaid competitors.

Therefore, the said acts and practices constitute an unfair method of competition.

XXXVIII

102. The use by respondents of the aforementioned unfair and deceptive statements, representations and practices has had, and now has, the capacity and tendency to mislead and deceive a substantial portion of the purchasing public into the erroneous and mistaken belief that such statements were, and are, true, and into

the purchase of substantial numbers of respondents' lots because of said mistaken and erroneous belief.

103. The aforementioned acts and practices, as herein alleged, were and are all to the prejudice and injury of the public and respondents' competitors and constituted, and now constitute, unfair methods of competition in or affecting commerce and unfair and deceptive acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act.

Decision and Order

The Federal Trade Commission having issued a complaint based upon alleged acts and practices of the respondents named in the caption hereto and having served such complaint upon respondents and having withdrawn the proceeding from the adjudication based upon a joint motion for withdrawal from adjudication filed by complaint counsel and counsel for respondents; and

The respondents and counsel for the Commission having executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and the complaint should have issued stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 3.25(f) of its Rules, now in further conformity with the procedure prescribed in Section 3.25(f) of its Rules, the Commission hereby makes the following jurisdictional findings, and enters the following order:

1. Respondent Cavanagh Communities Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 444 Brickell Ave., Miami, Flordia.

Respondent Cape Cave Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 444 Brickell Ave., Miami, Florida.

Respondents Cavanagh Marketing Corporation, Cavad, Inc., Wellington Orient, Inc., Miami Beach Vacations, Inc., Palm Beach Investment Properties, Inc., and Perdido Bay Management Corp. are corporations organized, existing and doing business under and by virtue of the laws of the State of Florida, with their principal offices and places of business located at 444 Brickell Ave., Miami, Florida.

Respondent Universal Properties, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Ohio, with its principal office and place of business located at 444 Brickell Ave., Miami, Florida.

Respondents Joseph Klein and Arthur Meltzer are now and/or have been officers and directors of respondent Cavanagh Communities Corporation and several of the other corporate respondents. Their address is 444 Brickell Ave., Miami, Florida.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

Order

As used in this order, the following definitions shall apply:

"Property Report" shall include documents entitled "Public Property Report," "Public Offering Statement," "Subdivision Public Report," "Offering Statement," "Prospectives," "Prospectus," "Public Report," and any other document providing information regarding the purchase of land in general or a specific subdivision in particular which is required by federal or state law to be distributed to prospective purchasers or purchasers of land.

"Respondents' subdivision" refers to a subdivision:

(a) The land in which is being sold by one or more of the respondents; (b) for which one or more of the respondents is a mortgagee and exercises control over the advertising, offering for sale, or sale of land in the subdivision; (c) for which one or more of the respondents is the registrant with any state or federal agency which regulates land sales; (d) for which one or more of the respondents is a party to the contracts of sale for lots therein which have been or are being sold to purchasers.

"Land" or "lots" shall mean any real property located in one of respondents' subdivisions, but shall exclude (i) land or lots upon which a residential or commercial structure is located; (ii) land or lots which is or are sold together with or under a contract to construct a house or other building thereon within 24 months of the date of sale of the land or lots; and (iii) land or lots sold to a purchaser pursuant to a single contract for a sum in excess of $50,000.

"Commission" shall refer to the Federal Trade Commission and/or its duly authorized representatives and employees.

As used in this order, a requirement to cease and desist from representing or misrepresenting shall include representing or misrepresenting directly or by implication, and by any manner or means.

No provision of this order shall be construed as limiting the application of any other paragraph of this order unless such limitation is *expressly* provided for in this order.

It is ordered, That respondents Cavanagh Communities Corporation, Cape Cave Corporation, Cavanagh Marketing Corporation, Cavad, Inc., Universal Properties, Inc., Wellington Orient, Inc., Miami Beach Vacations, Inc., Palm Beach Investment Properties, Inc., and Perdido Bay Management Corp., corporations, and their officers, and their subsidiaries and the said subsidiaries' officers, and Joseph Klein and Arthur Meltzer, individually, and respondents' successors, assigns, agents, representatives and employees, directly or through any corporate or other device in connection with the advertising, offering for sale, or sale of real property in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. (a) Failing to disclose, clearly and conspicuously, in any written or oral invitation or other communication concerning any event or activity, including but not limited to dinner parties or other similar gatherings, contests, or awards of free or low cost gifts, vacations, or sightseeing tours, or any other goods or services, which is in any manner a part of a plan or procedure to sell land, the following statement:

> The purpose of [the event or activity] is to sell you land in [name of State in which land is located] priced from approximately [price which is at or above the price, including assessments, of at least 5% of the lots being offered for sale].

(b) If the invitation or communication referred to in subparagraph (a) above is in writing, such disclosure shall be in writing and shall be made clearly and conspicuously in the invitation or communication; if such invitation or communication is oral and delivered in person, such disclosure shall be both oral and in writing and shall be made clearly and conspicuously and in conjunction with the invitation or communication; if such invitation or communication is made by telephone, such disclosure shall be made orally and clearly and conspicuously in the telephone invitation or communication, and in writing. All written disclosures shall be received by the prospective purchaser prior to the event or activity.

(c) Misrepresenting the true nature and purpose of any event or activity, including but not limited to dinner parties or other similar gatherings, contests, awards of free or reduced price gifts or vacations, and sightseeing tours.

2. Failing to set forth as the title of any contract for the purchase of land, in boldface type of a minimum size of 24 points, the following langauge: "CONTRACT FOR THE PURCHASE OF LAND."

3. (a) Failing to print the following in 12-point boldface type as the only writing, in addition to that required by paragraph 2 above, subparagraph 3(b) below if applicable, and, at respondents' option, the name of the seller, the subdivision in which the lot is located, the contract number, and/or the date of the contract, on the first page of all contracts for the sale of land:

> This is a contract by which you agree to purchase land.
>
> The future value of this land, as well as all undeveloped real estate, is speculative and risky.
>
> It is unlikely that the value of the land will increase or that you will be able to resell your land without significant community development and population growth, which may not occur for for a number of years, if at all.
>
> [Subparagraph 3(b)(i) Disclosure]
>
> [Subparagraph 3(b)(ii)-(vi) Disclosures]
>
> [Subparagraph 3(b)(vii) Disclosure]
>
> You have 10 business days in which to cancel this contract and get all your money back. Carefully read the property report (sometimes called an offering statement, public report or prospectus) which must be given to you when you sign this contract. It explains many important facts about your lot. You should go over this contract and the property report with a qualified professional before your 10 days are up.

Provided, however, that in the event no property report is required for the lot or lots being offered for sale, the following paragraph shall be used in lieu of the last paragraph of the above disclosure:

> You have 10 business days in which to cancel your contract and get all your money back. You should go over this contract with a qualified professional before your 10 days are up.

(b) Failing to print in the form and place set out in subparagraph (a) above, such of the following statements as are applicable:

(i) For contracts for the sale of lots whose elevations are below the 100-year flood level established by the United States Department of Housing and Urban Development, or are otherwise subject to flooding, add the following:

> This land [, as most of coastal Florida,] is susceptible to flooding. Unusual or costly building requirements may be applicable.

Provided, however, that the bracketed language must be omitted when the subdivision being advertised, if other than a Rotonda subdivision, is not located within five miles of the Atlantic or Gulf Coasts of Florida; and *further provided* that, in the event respondents have a contractual obligation, in accordance with paragraph 15 below, to develop all lots being sold within the subdivision being advertised at sufficient elevations with regard to the established 100-year flood levels to enable purchasers to build on their lots with no extra expense or unusual building requirements, then the disclosure required by this subparagraph may be omitted.

(ii) For contracts for the sale of lots to which electricity and/or telephone service are not available at the time of sale and to which respondents or any other party, including any utility company franchised or regulated by a government agency, are not legally obligated to provide or assure the availability of electricity and/or telephone service, add the following, including whichever of the bracketed language is applicable:

> No plans have been made to make [electricity and telephone service] available to your lot.

(iii) For contracts for the sale of lots to which electricity and/or telephone service will be provided only upon the payment of a line extension fee, add the following, including whichever of the bracketed language is applicable:

> The payment which must be made to a utility company in order to get [electricity and telephone service] to your lot may be very high.

(iv) For contracts for the sale of lots to which respondents or any other party, including any utility company franchised or regulated by a government agency, are not legally obligated to provide or assure the availability of potable water and/or sewage disposal, add the following, including whichever of the bracketed language is applicable:

> [Drinkable water and sewage disposal] may not be available to your lot.

(v) For contracts for the sale of lots to which the legal obligation of respondents or any other party regarding the roads to be provided to such lots is limited to the installation of unpaved roads with no maintenance obligations, add the following, including the bracketed language if the roads to the lot being offered for sale have not been constructed at the time of sale:

> [The land you are purchasing is undeveloped land.] Your lot will be accessible, if at all, only by unpaved, unmaintained roads which may become impassable.

(vi) For contracts for the sale of lots to which respondents or any other party are legally obligated to provide only drainage and/or unpaved roads with no maintenance obligations, and to which electricity and telephone service are not available at the time of sale, add the following, including the bracketed language if such roads have not been constructed at the time of sale, in lieu of the disclosures in subparagraphs (ii)-(v) above:

> [The land you are purchasing is undeveloped land.] Electricity, water, sewage disposal, and telephone service are not planned and may be impossible to obtain. Your lot will be accessible, if at all, only by unpaved, unmaintained roads which may become impassable. Your lot has virtually no use at present or in the foreseeable future.

(vii) For contracts for the sale of lots to which respondents or any other party are legally obligated to provide only drainage, or no improvements at all, add the following in lieu of the disclosures in subparagraphs (ii)-(vi) above:

> The land you are purchasing is completely undeveloped. No roads or other improvements are planned, and your lot is probably inaccessible by conventional means of transportation. Your lot has virtually no use at present or in the foreseeable future.

(viii) For contracts for the sale of lots which are designated or zoned for any use other than single family residential, add the following:

> The designation or zoning of a lot as [indicate lot's designation or

zoning classification, *e.g.*, multiple family residential] may have no bearing on its value.

4. Failing, in connection with the sale of land, to disclose, clearly and conspicuously, in all sales presentations, promotional materials, and advertisements other than billboards primarily containing road directions to a subdivision, the following statement:

Since land values are speculative and risky, you should consult a qualified professional before buying. It is unlikely that you will be able to resell your land or resell it at a profit without significant community development and population growth, which may not occur for a number of years, if at all.

Provided, however, that in lieu of the above statement, the following statement may be used in (i) radio or television advertisements of 30 seconds or less; (ii) magazine advertisements of 1/8 page or less; and (iii) newspaper advertisements of 1/8 page or less:

Remember–buying land is risky! Consult a qualified professional before buying!

5. Failing to furnish the purchaser of land with a fully completed copy of any contract at the time of its signing by the purchaser, which is in the same language, *e.g.*, Spanish, as that principally used in the oral sales presentation, if any, and which shows the date of the transaction and contains the name and address of the respondent corporation which is the contracting party, provided that the contract need not at this time contain the signature of respondents.

6. Failing to print all conditions and provisions of any contract for the sale of the land in a clear and conspicuous manner, and, where any conditions or provisions are set forth on the reverse side of said contract, failing to indicate in a clear and conspicuous manner at the bottom of the front side of said contract that the purchaser should carefully examine the reverse side.

7. (a) Failing to furnish each purchaser of land, at the time he or she signs the contract, with a completed form in duplicate captioned "NOTICE OF CANCELLATION" which shall contain in boldface type of a minimum size of 10 points, except for the language designated as "Note" relating to notification, which may appear in any type setting which is clear and conspicuous, the following statement in the same language, *e.g.*, Spanish, as that used in the contract:

NOTICE OF CANCELLATION

[*enter date of transaction*]

[*enter purchaser(s) name(s)*]

You may cancel this transaction, without any loss, expense, penalty or obligation, at any time prior to midnight of the 10th business day after the above date.

If you cancel, all payments made by you under the contract will be returned within 15 calendar days following receipt by the seller of your cancellation notice.

To cancel this transaction, mail or deliver a signed copy of this cancellation notice or any other written notice, or send a telegram to: *(name of applicable respondent),* at *(address of applicable respondent's place of business)* not later than midnight of *(date).*

> NOTE: Notification by mail shall be considered given at the time postmarked; notification by telegram shall be considered given at the time filed for transmission; and notification by other writing shall be considered given at the time delivered to respondent's place of business.

I (We) hereby cancel this transaction. (If only one purchaser signs this notice, it means he or she has the permission of any other purchasers to act for them.)

Purchaser's Signature *Date*

Purchaser's Signature

(b) Failing, before furnishing copies to the purchaser of the "Notice of Cancellation" set forth in subparagraph (a) above, to complete both copies by entering the name of the applicable respondent, the address of the applicable respondent's place of business, the date of the transaction, the purchaser's name, and the date, not earlier than the 10th business day following the date of the transaction, by which the purchaser must give notice of cancellation.

(c) Failing to inform each prospective purchaser orally, at the time the contract is signed, of the right to cancel as stated in subparagraph (a) above.

8. Requiring the purchaser of land to make a personal inspection of any property or the general vicinity thereof as a condition precedent to the cancellation of any contract or the refund of any moneys paid thereunder, unless:

(a) Respondents limit such inspection to the purchaser's lot and the subdivision in which it is located;

(b) The purchaser is actually taken to and shown his or her lot; *provided, however,* that if the purchaser's lot is not reasonably identifiable, and accessible by conventional means of transportation, during the inspection period provided by the contract, respondents shall extend the period until such time as the lot is identifiable and accessible, and shall notify the purchaser that his right to cancel his contract and receive a refund upon inspection of his lot has been so extended.

(c) In the event more than one purchaser has signed the contract, one purchaser is permitted to make the inspection as the representative of all the purchasers;

(d) Respondents provide the purchaser three business days following the date of inspection within which to cancel the contract or request the refund; and

(e) The purchaser's contract, as part of any provision requiring the purchaser to make a property inspection in order to cancel the contract and/or obtain a refund, clearly and conspicuously discloses the facts set out in subparagraphs (a)-(d) above.

9. (a) Failing to furnish each purchaser of land at the completion of the property inspection made in accordance with paragraph 8 above a completed form in duplicate captioned "NOTICE OF CANCELLATION" which shall contain in boldface type of a minimum size of 10 points, except for the language designated as "Note" relating to notification, which may appear in any type setting which is clear and conspicuous, the following statement in the same language, *e.g.,* Spanish, as that used in the purchaser's contract:

NOTICE OF CANCELLATION

[*enter date of inspection*]

[*enter purchaser(s) name(s)*]

You may cancel your contract, without any loss, expense, penalty or obligation, at any time prior to midnight of the third business day after the above date.

If you cancel, all payments made by you under the contract will be returned within 10 business days following receipt by the seller of your cancellation notice.

To cancel your contract, mail or deliver a signed copy of this cancellation notice or any other written notice, or send a telegram to: *(name of applicable respondent),* at *(address of applicable respondent's place of business)* not later than midnight of *(date).*

NOTE: Notification by mail shall be considered given at the time postmarked; notification by telegram shall be considered given at the time filed for transmission; and notification by other writing shall be considered given at the time delivered to respondent's place of business.

I (We) hereby cancel the contract. (If only one purchaser signs this notice, it means he or she has the permission of any other purchasers to act for them.)

Purchaser's Signature *Date*

Purchaser's Signature

(b) Failing to complete both copies of the "Notice of Cancellation" set out in subparagraph (a) above prior to furnishing them to the purchaser by entering the name of the applicable respondent and the address of its place of business, the date of the lot inspection, the names of the purchaser(s) making the inspection and the date, not earlier than the third business day following the date of said inspection, by which the purchaser(s) must give notice of cancellation.

10. (a) Failing in any instance where a timely notice of cancellation is received pursuant to subparagraphs 7(a) or 9(a) above, and said notice is not sufficient or proper in any manner and respondents do not intend to honor the notice, to immediately notify the purchaser by certified mail, return receipt requested, enclosing the notice, informing the purchaser of his or her error, and stating clearly and conspicuously that a sufficient notice properly signed must be mailed by midnight of the third day following the purchaser's receipt of said mailing if the purchaser is to obtain a refund.

(b) Failing to make refunds in accordance with the terms of any notices of cancellation timely received by respondents pursuant to subparagraphs 7(a), 9(a), or 10(a) above.

11. In connection with the refund provision set forth in paragraph 8 above, representing to prospective purchasers and purchasers that they may cancel their contracts and get refunds unless such is the fact and unless all conditions and limitations applicable thereto, including but not limited to the facts, where applicable, that the purchaser may be subjected to additional sales presentations while seeking to obtain a refund and that the purchaser must pay his or her transportation costs to and from the lot, are clearly disclosed in immediate conjunction therewith and with the same conspicuousness.

12. Transferring, selling assigning, or otherwise conveying any note or other evidence of indebtedness of the purchaser executed subsequent to the date this Order becomes final to a finance company or other third party prior to midnight of the 20th business day following the day the contract was signed.

13. (a) Offering for sale or selling lots which are represented as suitable for homesites unless the contracts for the sale of such lots contain a legal obligation on the part of respondents in accordance with paragraph 15 below, to provide or assure the availability of roads, electricity, telephone service, potable water, sewage disposal and where necessary, drainage, to such lots, installed or constructed to no less than those minimum government standards required for obtaining a building permit for a dwelling unit on such lots.

(b) Representing, in connection with the sale of land, that respondents will provide to a subdivision or lot therein, or that a subdivision or lot therein will have available, roads, electricity, telephone service, potable water, sewage disposal, or drainage, unless the contracts for the sale of lots in that subdivision, at the time of the representation, contain a legal obligation on the part of respondents, in accordance with paragraph 15 below, to provide or assure the availability of each such utility or improvement represented.

14. Representing, in connection with the sale of land, that respondents' subdivisions have or will have available, or that residents of respondents' subdivisions or lot purchasers therein have or will have the use of, any recreational facility, improvement, utility, amenity, or structure whether or not located in respondents' subdivisions [other than those utilities and improvements listed in subparagraph 13(b) above], including but not limited to golf courses, clubhouses, waterways, lakes, marinas, hotels, motels, shopping facilities, professional service facilities, beaches, and parks, unless

a) For representations of present availability or use:

(i) such representation is true, and (ii) the terms and conditions of availability to or use by purchasers and residents are clearly and conspicuously disclosed at the time of such representation, provided that such terms and conditions regarding retail stores and public establishments need not be disclosed if they are typical and customary for such stores and establishments, and (iii) at the time of the representation, respondents reasonably believe the recreational facility, improvement, utility, amenity, or structure will continue to be available in the foreseeable future.

b) For representations of availability or use in the future:

(i) the terms and conditions of availability to or use by purchasers and residents, including the date of completion or availability, are clearly and conspicuously disclosed at the time of such representation, provided that such terms and conditions regarding retail stores and public establishments–other than the date of completion–need not be disclosed if they are typical and customary for such stores and establishments; and

(ii) at the time of the representation, one of the following conditions is met:

(a) respondents are contractually obligated to provide such facility, improvement, utility, amenity, or structure in accordance with paragraph 15 below; or

(b) any other party is legally obligated to lot purchasers to provide such facility, improvement, utility, amenity, or structure, and respondents clearly and conspicuously disclose in immediate conjunction with such representation that respondents have no contractual obligation to make such facility, improvement, utility, amenity, or structure available or to assure its continued availability; or

(c) such facility, improvement, utility, amenity, or structure is at least 50% completed with completion reasonably anticipated by respondents within one year, and respondents have a reasonable basis to believe it will be available for use by purchasers and residents when completed and will continue to be so available in the foreseeable future.

15. (a) With respect to any recreational facility, improvement, utility, amenity, or structure which respondents are contractually obligated to provide or make available, failing to provide (i) through (v) below in the contract:

(i) an adequate description of each recreational facility, improvement, utility, amenity, and structure to be provided or available.

(ii) the date by which each such recreational facility, improvement, utility, amenity, and structure will be provided or available. For improvements and utilities, said date shall be a date certain not later than the date the purchaser's final scheduled payment would be due under the payment schedule contained in the applicable contract in use at the time of purchase which was offered to purchasers not paying on an accelerated basis. Provided that in the case of central water or central sewage facilities, the contract may provide either A or B below:

(A) said facilities will be installed within one year after respondents' receipt of written notice from the purchaser that he or she intends to build on his or her lot, provided that if the contract provides for this alternative, such contract may also provide, where applicable, the roads to such lot do not have to be paved until the expiration of said one year period; or

(B) said facilities will be available when a stated level of population density in a specified area is achieved, provided that the contract further states, in accordance with subparagraph (b) below, that respondents assure the availability of potable water by means of a well and/or sewage disposal by means of a septic tank.

(iii) the dollar amount of all costs, fees, and/or assessments which a purchaser must pay for the construction and/or installation of each recreational facility, improvement, utility, amenity, and structure; *provided, however,* that if the costs, fees and/or assessments so represented are estimates, (1) the contract shall disclose this fact and that these costs, fees, and assessments may actually be higher. Said disclosure shall be made clearly, in immediate conjunction with the representation of the costs, fees, and/or assessments and with the same conspicuousness as such representation; and (2) such estimates must be substantiated in writing at the time they are represented by competent and reliable engineering studies which shall include a reasonable allowance for inflation. Such substantiation shall be maintained for at least three years after all fees, costs and/or assessments which it relates to have been paid by the purchaser.

(iv) if under the terms of the contract the purchaser may be required to pay for the installation of a well and/or septic tank, a provision stated as follows, including whichever of the bracketed language is appropriate:

In the event that the purchaser determines, within five years after his payments are completed or the deed has been issued, whichever is later, that a [well or septic tank] cannot be used on his or her lot, the seller shall refund to the purchaser the cost of the test which determined that the [well or septic tank] cannot be used, provided that in the event the cost of the test is substantially higher than the prevailing rate for such test by qualified businesses in the vicinity of the applicable subdivision, the seller may limit such refund to the prevailing rate for such test.

It shall be the responsibility of the purchaser, within 90 days after determining that [either a well or septic tank] cannot be used on his or her lot to notify the seller of this fact and request a refund of the cost of the test which determined that the [well or septic tank] cannot be used.

(v) a provision stated as follows:

In the event the subdivision or the lot which is the subject of the contract has not been provided with or does not have available any contracted-for improvement or utility, or there has been a material failure to provide or make available any contracted-for recreational facility, amenity or structure, within six months of the time specified in the contract plus the actual number of days of any delay caused by any strike or work stoppage beyond respondents' control, or an act of God, the seller will, within 60 days after the expiration of the applicable time period, provide the purchaser by certified mail, return receipt requested, with notice of such failure to provide or such unavailability, and of the purchaser's right to a refund of all moneys paid (including but not limited to principal, interest, taxes, and assessments) under the contract plus interest at the rate of 7% per annum computed from the date of default; *provided, however,* that at the time the purchaser is notified of such refund, the purchaser may also be offered the option of selecting, in lieu of such refund, an exchange of the purchaser's lot, at no additional cost to the purchaser, for another lot to which all contractual obligations of respondents have been met, which was or would have been of at least equal price on the date the purchaser's contract was signed, which is located in the same subdivision or community, is at least the same size, has the same zoning classification, has the same utilities and improvements as respondents were obligated to provide under the original contract, and is located no further from the same or substantially similar recreational and commercial facilities and amenities as the original lot.

(b) If under the terms of the contract potable water and/or sewage disposal are to be provided for any period of time by means of a well and/or septic tank, in the event a well or septic tank cannot be used on such lot within five years after the purchaser completes his or her payments or receives a deed, whichever is later, respondents, within 60 days after determining or receiving notice of that fact, shall comply with either (i) or (ii) below, at respondents' option:

(i) Contract with the purchaser to provide central sewage and/or central water to the lot not later than one year after determining or receiving notice that a well and/or septic tank cannot be used on the lot; *provided, however,* that if the deed to the lot had not been issued at the time respondents reach such a determination or receive such notice respondents may provide central sewage and/or central water to the lot at any time within one year from the date the purchaser's final scheduled payment is due under the contract.

(ii) Offer the purchaser of a refund of all moneys paid (including but not limited to principal, interest, taxes, and assessments) under the contract plus interest at the rate of 7% per annum computed from the date of default; *provided, however,* that at the time the purchaser is offered such refund, the purchaser may also be offered, in lieu of such refund, an exchange of the purchaser's lot for another lot to which all contractual obligations of respondents have been met, which was or would have been of at least equal price on the date the purchaser's contract was signed, and which is located in the same subdivision or community, is at least the same size, has the same zoning classification, has the same utilities and improvements as respondents were obligated to provide under the original contract, and is located no further from the same or substantially similar recreational and commercial facilities and amenities as the original lot.

(c) Failing to notify the purchaser of his or her right to a refund or exchange as set out in subparagraphs (a)(v) and (b) above; failing to provide central sewage and/or central water to the purchaser's lot as provided in subparagraph (b)(l) above; and failing to make the refund or exchange provided for in subparagraphs (a)(v) and (b) above within 30 days of receipt of the purchaser's request for such refund or exchange; *provided, however,* that in the event respondents are obligated under this paragraph to make refunds exceeding $500,000 as a result of a single default common to many lots, it shall not be a violation of this order for respondents to prorate such refunds, with interest at a rate of 7% per annum from the date of default, over a period of five years from the date of default.

16. (a) Representing that a central sewage and/or water system will be available when a stated level of population density in a specified area is achieved unless it is clearly and conspicuously disclosed in immediate conjunction therewith and with the same conspicuousness (i) that purchasers will be required to use a well and/or septic tank if they build on their lots before said level of population density is reached, and (ii) the approximate cost to the purchaser of installing a well and/or septic tank.

(b) Failing to clearly and conspicuously disclose in writing the substance of paragraph 15(a)(iv) above, at the time the deed is issued, to each purchaser of a lot to which a central sewage and/or water system will be made available when a stated level of population density in a specified area is achieved.

(c) Collecting assessments prior to the start of construction for a central sewage and/or a central water system which is required to be provided or made available when a stated level of population density is achieved unless the following conditions are complied with:

(i) collection of such assessments is begun no sooner than two years prior to the commencement of construction of such system(s);

(ii) such assessments are placed in escrow;

(iii) in the event construction does not commence within two years after the collection of assessments has begun, all such assessments shall be refunded to the purchasers from whom they were collected with interest at a rate of 7% per annum from the date each assessment payment was received until the date such refund was made; and

(iv) in the event the central sewage and/or central water system has not been provided or made available to a lot within five years after the collection of assessments has begun plus the actual number of days of any delay caused by an act of God or a strike or work stoppage beyond respondents' control, all such assessments shall be refunded to the purchasers of such lots with interest at a rate of 7% per annum from the date each assessment payment was received until the date such refund is made.

Provided, however, that in the event state or federal regulations require that assessments collected pursuant to this subparagraph of the order be placed in an escrow account subject to the control of a state or federal agency, respondents shall use their best efforts to provide in any agreement for refund provisions in accordance with subparagraphs (c)(iii) and (c)(iv) above or otherwise to obtain a legally binding commitment from such state or federal agency to permit respondents to comply with subparagraphs (c)(iii) and (c)(iv) above.

(d) Failing to make refunds within 90 days after the expiration of the two year period described in subparagraph (c)(iii) above and after the expiration of the five year period described in subparagraph (c)(iv) above.

17. (a) Representing to a prospective purchaser or to a purchaser prior to the time a deed for his or her lot is issued, that respondents will construct or cause to be constructed a building on the prospective purchaser or purchaser's lot or will rent or sell such a building or units therein for the benefit of the purchaser, unless respondents offer to enter into a contract with the purchaser to do so or offer the purchaser the right to an option to enter into such a contract at a future date, on mutually agreeable terms, and unless that contract contains a provision which gives the prospective purchaser or purchaser, in the event respondents default in their obligation to build or have built, rent or sell such building or units therein, the right to cancel the contract for the purchase of the lot upon which said building has been or was to be constructed and receive a refund of all monies paid thereunder, including but not limited to payments of principal, interest, taxes, assessments, and recording costs, plus interest at the rate of 7% per annum from the date of default.

(b) Failing within 60 days of receipt of a prospective purchaser or purchaser's request for a refund made in accordance with subparagraph (a) above to make the refund so requested.

18. Soliciting or obtaining the purchaser's assent to or otherwise imposing any condition, waiver or limitation upon the right of a purchaser to a refund or exchange as set forth in paragraphs 15 and 17 of this order; *provided, however,* that:

(i) respondents may require purchasers to request a refund or exchange within a stated time period of not less than 90 days after the purchaser is notified by respondents of their default under the contract;

(ii) this paragraph shall not preclude respondents from offering a purchaser additional alternatives which may be selected, at the purchaser's option, in lieu of a refund or exchange; and

(iii) in the event the purchaser has received a deed or other evidence of title in the contracted-for property other than a contract, or has recorded the contract, the purchaser must, as a condition of obtaining such refund or exchange, reconvey to the seller such interest by deed and/or other appropriate instruments provided by respondents.

19. (a) Failing to include in all contracts for the sale of land entered into on or after the date this order becomes final:

(i) a provision limiting the moneys paid by a purchaser under the contract to be forfeited in the event of the purchaser's default to an amount not greater than 40% of the "cash price;" and

(ii) a provision stating that, in the event the purchaser fails to make any payment required under the contract, the purchaser shall be deemed in default not later than six months after the payment was due, provided that the default has not been cured prior to that time; *provided, however,* that respondents shall be permitted to delay declaring a delinquent purchaser in default if so requested by the purchaser.

(b) Failing to refund to purchasers, in accordance with the contract provision set forth in subparagraph (a)(i) above, all moneys paid under the contract, including but not limited to principal, interest, taxes, and assessments which in the aggregate exceed 40% of the "cash price," within 60 days after the purchaser is deemed to have defaulted; *provided, however,* that it shall not be a violation of this order for respondents to pro-rate all such refunds with interest at the rate of 8% per annum from the date of default, over a period of three years from the date of default or, in the event of a refund of $1500 or more to a single purchaser, over a period of five years from the date of default for that purchaser's refund; and *further provided,* that this subparagraph shall not preclude respondents from offering a defaulting purchaser additional alternatives which may be selected at the purchaser's option, in lieu of a refund.

For purposes of this paragraph of the order, "cash price" shall be the amount of money described in the purchaser's contract as the "cash price" in accordance with Section 226.2(n) of Truth in Lending Regulation Z, 12 CFR 226.

20. In connection with the sale of land:

(a) Failing to disclose, clearly and conspicuously in 10-point boldface type in printed advertisements and promotional materials, and clearly and conspicuously in sales films and other audio-visual materials used during sales presentations, for subdivisions in which at least 15% of the platted lots are, at the time of sale, at elevations below the 100-year flood level established by the United States Department of Housing and Urban Development, or are otherwise subject to flooding, the following:

> This land [, as most of coastal Florida,] is susceptible to flooding. Unusual or costly building requirements may be imposed.

Provided, however, that the bracketed language must be omitted when the subdivision being advertised, if other than a Rotonda subdivision, if not located within five miles of the Atlantic or Gulf Coasts of Florida; and *further provided,* that in the event respondents have a contractual obligation, in accordance with paragraph 15 above, to develop all lots being sold within the subdivision being advertised at sufficient elevations with regard to the established 100-year flood levels to enable purchasers to build on their lots with no extra expense or unusual building requirements, then the disclosure required by this subparagraph may be omitted.

(b) In the event a lot represented as suitable for a homesite whose elevation is below the 100-year flood level established by the United States Department of Housing and Urban Development, or which is otherwise subject to flooding, cannot lawfully be used, even with pilings, fill dirt, or other usual and customary building techniques, if any, as a homesite at the time the deed should issue due to zoning regulations or other laws related to the lot's elevation or susceptibility to flooding, respondents shall offer to the purchaser of such lot one of the following, or an option of selecting from one of the following:

(i) a refund of all moneys paid (including but not limited to principal, interest, taxes, and assessments) under the contract plus interest at the rate of 7% per annum computed from the date of default; or

(ii) an exchange of the purchaser's lot for another lot to which all contractual obligations of respondents have been met, which was or would have been of at least equal price on the date the purchaser's contract was signed, and which is located in the same subdivision or community, is at least the same size, has the same zoning classification, has the same utilities and improvements as respondents were obligated to provide under the original contract, and is located no further from the same or substantially similar recreational and commercial facilities and amenities as the original lot.

Provided, however, that this subparagraph of the order should not be construed to limit any additional rights and remedies the purchaser may have under his or her contract.

(c) Failing to offer the purchaser the refund or exchange set out in subparagraph (b) above within 90 days of determining that the lot cannot lawfully be used as a homesite at the time the deed should issue, and failing to make the refund or exchange in accordance with subparagraph (b) above within 30 days of receipt of the purchaser's request for such relief.

21. (a) Making any statement or representation in writing, or orally in sales films or other audio-visual materials used during sales presentations, concerning the purchase price of land without clearly disclosing in immediate conjunction therewith and with the same conspicuousness as such statement or representation the nature and estimated amount of any additional assessments and other improvement costs which must be paid by the purchaser to respondents or any third party; *provided, however,* that this subparagraph shall not apply to the disclosure required by subparagraph 1(a) above.

(b) Failing to clearly disclose in the contract, in immediate conjunction with the purchase price of the lot and with the same conspicuousness:

(i) the nature and estimated amount of any assessments and other improvement costs; and

(ii) a reference to the other items for which payments are required, including but not limited to utilities not included in the assessments, fill dirt, pilings, conservation associations, property taxes, and canal maintenance, which must be paid by the purchaser to respondents or any third party in order to purchase such lot and make it usable for the purposes represented.

22. (a) Requiring purchasers of lots in respondents' subdivisions to join a Conservation Association or any other association, society, league, corporation, or other entity which can require its members to pay assessments or other fees [hereinafter in paragraph 22 referred to as a Conservation Association], or including in such purchasers' contracts or in the deeds of restriction provisions whereby they become members of a Conservation Association, unless the declaration, by-laws or other regulations governing the Conservation Association: (i) give each purchaser a vote in association matters at the time he or she becomes a member; (ii) apportion all votes in a fair and equitable manner, provided that land which has not been platted into lots shall not be apportioned or otherwise used as a basis for determining a member's voting rights; and (iii) provide nonresident members a reasonable means to participate and vote in Conservation Association matters.

(b) Failing to disclose to all prospective purchasers of land in subdivisions where a Conservation Association has been or is planned to be established, clearly and conspicuously in writing:

(i) the circumstances under which they become members of the Conservation Association;

(ii) that the Conservation Association may assess such purchasers for the maintenance of and capital improvements to the common properties in the subdivisions in which their lots are located, if such is the fact;

(iii) the specific items, and the assessment per lot for each such item, for which association members have been assessed over the past three years; and

(iv) the estimated time period during which respondents will be the sole voting member or will otherwise have voting control of the Conservation Association.

23. Representing any of the following to any prospective purchaser or purchaser of land:

(a) That the purchase of a lot in one of respondents' subdivisions is a way to insure financial security, to deal with inflation, or to become wealthy.

(b) That real estate is a good or safe investment.

(c) That land in respondents' subdivisions is being offered for sale for investment purposes or is suitable for investment purposes.

(d) That the purchase of a lot in one of respondents' subdivisions is a good or safe investment.

(e) That land is becoming scarce; *provided, however,* that this subparagraph shall not prohibit any representations permitted under paragraph 43 below.

Provided, however, that this paragraph shall not prohibit any representations permitted under paragraph 25 below.

24. Representing to any prospective purchaser or purchaser of land that the prices for land in respondents' subdivisions periodically rise, or that such prices have increased, are increasing, or may or will increase, unless the following is clearly discosed in immediate conjunction with such representations and with the same conspicuousness:

> Price increases are made at the seller's discretion and do not mean that the land has increased in value or that a purchaser can resell a lot at the higher price or at any price.

Provided, however, that in the case of oral representations, such disclosures shall be made both orally and in writing.

25. Representing to any prospective purchaser or purchaser of land that the value of or demand for any land, including lots in respondents' subdivisions, has increased, is increasing, or will or may increase, or that purchasers have made, are making, or will or may

in the future make, a profit through the purchase of a lot or lots in respondents' subdivisions.

Provided, however, that respondents may truthfully represent to a prospective purchaser at the time of sale, or to a purchaser at the time of a property inspection:

(a) The price at which vacant lots in respondents' subdivisions have been resold by the original purchaser or subsequent purchasers if the following conditions are met:

(i) Respondents and/or their agents, representatives or employees were not parties (*i.e.,* seller or purchaser) to the resale;

(ii) the resale was an arm's-length transaction for cash or its equivalent;

(iii) the resale was of a lot in the same subdivision or community as the lot which is being offered for sale to the prospective purchaser or which was sold to the purchaser. For the purposes of this subparagraph, the term "community" shall mean two or more adjacent subdivisions sold pursuant to a common promotional plan;

(iv) the resale lot has the same zoning or use classification as the lot which is being offered for sale to the prospective purchaser or which was sold to the purchaser;

(v) the site classification (*e.g.,* interior lot, greenbelt, canal, riverfront, golf course) of the resale lot is comparable or less valuable than that of the lot which is being offered for sale to the prospective purchaser or which was sold to the purchaser;

(vi) the resale lot is similar in size or smaller and has the same or lesser improvements and utilities, as the lot which is being offered for sale to the prospective purchaser or which was sold to the purchaser;

(vii) at least five resales of lots meeting the conditions set out in this subparagraph have occurred within the two years prior to the representation;

(viii) the resale price does not exceed by more than 20% the mean or median price of all resales meeting the conditions set out in this subparagraph which occurred within two years of the representation. Respondents shall not be considered to be in violation of this subparagraph if the resale price they are representing exceeds the mean or median resale price by more than 20% solely due to resales which occurred within six months of the representation; and

(ix) the following is clearly disclosed in immediate conjunction with the representation and with the same conspicuousness:

> The fact that other lots in this subdivision have been resold does not mean that there is a resale market, or that you will be able

> to resell your lot at any price. Check with a local real estate broker for resale information.

Provided, however, that in connection with the sale of land in the Rotonda subdivisions, respondents shall make no representations of the price of resales in the Oakland Hills segment of Rotonda West except with respect to sales of Oakland Hills lots, and shall not represent the price of resales in the other segments of Rotonda West in connection with the sale of lots in the other Rotonda subdivisions.

(b) the price at which any lot in a competing subdivision which is similar to the lot which is being offered for sale to the prospective purchaser or which was sold to the purchaser is currently being sold, or the last price at which any such lot was sold in a transaction to which respondents and/or their agents, representatives, or employees were not parties (*i.e.*, seller or purchaser), if the following is clearly disclosed in immediate conjunction with the representation and with the same conspicuousness:

> The fact that lots in other subdivisions are being sold does not mean that you will be able to resell your lot at the same price or at any price. Check with a local real estate broker for resale information.

Respondents shall not be considered to be in violation of this subparagraph if the sales price represented is not current or the resale price represented is not the last such price solely due to price changes or new resales occurring within six months of the representation.

Respondents shall maintain, for a period of three years after making any representation pursuant to subparagraphs (a) or (b) above, data sufficient to substantiate each such representation, and shall make such data available during normal business hours to the Commission for inspection and copying.

26. Misrepresenting the past, present, or future sales price of lots in respondents' subdivisions.

27. Making any representation in connection with the sale of land which refers to or concerns investment in stocks, insurance, banks, or any other form of investment other than land in respondents' subdivisions and other comparable subdivisions.

28. Making representations in connection with the sale of land concerning or comprised of statistics or trends of population, employment, business, or industry, or making representations concerning or comprised of other statistics or trends, unless respondents have at the time of making such representations, and maintain for three years thereafter, a reasonable basis to believe:

(i) For representations concerning or comprised of statistics or trends regarding past or present events, that such representations are true; and

(ii) For representations concerning or comprised of statistics or trends regarding future events, that such statistics or trends will occur as represented.

A reasonable basis shall consist of current, relevant, and objective statistical or economic data or studies, where such data are collected or such studies are conducted in accordance with accepted applicable demographic, economic, and/or statistical principles.

29. Representing that respondents may or will buy back lots from or resell lots for purchasers, or may or will set up a resale division; or misrepresenting that purchasers will be able to sell their lots or their interest therein.

30. Representing that respondents have developed new towns or communities, or are well-known, experienced, or highly regarded community developers; or misrepresenting respondents' business experience, reputation, or financial conditions.

31. Representing that respondents' subdivisions or waterfront property therein provide access by boat to the Atlantic Ocean, Gulf of Mexico, or any other body of water, or that canals, lakes, or other waterways are navigable or can be used for any recreational activity, unless such is the fact and unless all material qualifications pertaining to such access, navigability or use, including but not limited to the size or type of boats which can obtain access to open water or navigate the waterways and speed limits which may be established, are clearly disclosed in immediate conjunction therewith and with the same conspicuousness as such representation.

32. Misrepresenting the mileage, percentage, or other amount or proportion of any recreational facility, improvement or utility, including but not limited to roads, curbs, gutters, utility lines, and water or sewage mains, which has been completed, is under construction, or will be constructed in respondents' subdivisions.

33. Using similar names for subdivisions in which the recreational facilities, improvements, utilities, and amenities available in each such subdivision are not substantially identical; *provided, however,* that respondents shall not be obligated to rename any currently platted subdivision.

34. (a) Making any representation concerning Palm Beach Gardens in any advertisement, promotional material, or sales presentation for any land located in Palm Beach or Martin Counties, Florida.

(b) Making any representation concerning any recreational facility, improvement, utility, or amenity available or located in a city, community, subdivision or other geographic area during a sales presentation or in an advertisement or promotional material relating to one or more of respondents' subdivisions at which similar recreational facilities, improvements, utilities, or amenities have not been provided and there is no contractual obligation to so provide or assure the availability of, unless respondents disclose in immediate conjunction therewith and with the same conspicuousness as such representation that similar recreational facilities, improvements, utilities, or amenities will not be provided at respondents' subdivision or subdivisions to which the sales presentation, advertisement, or promotional material relates.

35. Representing:

(a) That Rotonda West, Rotonda Shores, Rotonda Lakes, Rotonda Heights, Rotonda Meadows, Rotonda Springs, Rotonda Sands, or Rotonda Villas have been or will be provided, either singly or in conjunction with one or more of the other Rotonda subdivisions, with a multimillion dollar clubhouse or clubhouses, underground electric or telephone lines, concrete curbs and gutters, sidewalks, a fully developed central core, a tennis clinic, more than two golf courses, or a private island.

(b) That Twin Lakes Country Club and Estates will be provided with gas lines.

(c) That Paradise Hills will be developed in any manner.

(d) That Palm Beach Heights has been or will be provided with any recreational facility, improvement, utility or amenity other than unpaved, unmaintained dirt roads and drainage.

(e) That any lot in Perdido Bay Country Club Estates will be developed prior to the date for completion of improvements stated in the contract.

Provided, however, that this paragraph shall not preclude respondents from making any of the representations prohibited by subparagraphs (a)-(e) above if, at the time the representation is made, respondents have a contractual obligation in accordance with paragraph 15 above to develop the subdivision as represented.

36. (a) Representing that any recreational facility, improvement, utility, amenity, or residential structure is planned for a subdivision or part thereof when such plans have been altered, abandoned, superseded, postponed, or otherwise will not be completed as represented.

(b) Representing that any recreational facility, improvement, utility, or amenity has been provided or is available at a subdivision or part thereof when such recreational facility, improvement, utility, or amenity has been closed or is no longer available for use.

37. In the event that the development plans for any subdivision, including plans for any recreational facility, improvement, utility, amenity, or residential structure, are materially altered, abandoned, or otherwise will not be completed as represented, failing to disclose such alteration, abandonment, or other change in plans within 90 days of such event to each purchaser of a lot in the subdivision in which the development plans were to occur, and to each purchaser in any other of respondents' subdivisions which is located within 25 miles of the subdivision in which the development plans were to occur; *provided, however,* that in connection with development plans in the Rotonda subdivisions:

(i) if the subdivision in which the development plans were to occur is Rotonda West, then such disclosure shall be made to all purchasers of lots in each of the Rotonda subdivisions;

(ii) if the development plans concerned a recreational facility, improvement, utility, amenity, or residential structure which was to serve more than one of the Rotonda subdivisions, then such disclosure shall be made to all purchasers of lots in each such subdivision;

(iii) if the development plans were to occur in a subdivision other than Rotonda West, and the recreational facility, improvement, utility, amenity, or residential structure was not intended to serve more than one Rotonda subdivision, then such disclosure shall be made to all purchasers in the one subdivision affected.

Notwithstanding the above, if the change in development plans directly affects 100 or fewer lots, will have no impact on the overall development of a subdivision or community, and does not concern a recreational facility, amenity, or residential structure which was represented in any advertisement or promotional material for respondents' land, such disclosure is required to be made only to the purchasers of the lots directly affected.

38. Misrepresenting the past, present, or future development plans of state of development of any subdivision or part thereof, including but not limited to the recreational facilities, improvements, utilities, amenities, or residential structures therein; or misrepresenting the size, qualities, characteristics, location, or usefulness of any subdivision or part thereof.

39. (a) Representing that any person who acquired real property in any of respondents' subdivisions free, for a nominal cost, at a price substantially below fair market value, or as payment for services, purchased said property or chose to buy or live in said subdivision

rather than in other places; or misrepresenting how or why a person acquired property in any of respondents' subdivisions.

(b) Representing that any person who acquired real property in any of respondents' subdivisions free, for a nominal cost, at a price substantially below fair market value, or as payment for services, acquired such property and/or lives in such subdivision unless it is clearly disclosed in immediate conjunction with such representation and with the same conspicuousness that the person acquired his property free, for a nominal cost, at a price substantially below fair market value, or as payment for services, whichever is appropriate.

40. (a) Representing that Ed McMahon is an officer of any of the corporate respondents.

(b) Representing that any well-known person is an officer or employee of any of the corporate respondents unless such representation is true and unless said person performs duties commensurate with the office and spends a substantial portion of his time in such corporate capacity; *provided, however,* that respondents shall be permitted to make representations otherwise prohibited by this subparagraph when such representations are required by law, in the form and manner specifically prescribed by such law; and *further provided,* that documents containing such prescribed representations shall not be distributed to prospective purchasers or purchasers unless required by such law.

(c) Misrepresenting that any well-known person lives in one of respondents' subdivisions, owns stock in any of the corporate respondents, or is a substantial investor in any of the corporate respondents or in any of respondents' subdivisions.

41. Representing that General Electric Co. or its affiliates, subsidiaries, or divisions planned, designed, engineered, or developed any subdivision or part thereof, or put its entire corporate resources behind any subdivision; or misrepresenting the participation of General Electric Co. or any other company in respondents' subdivisions.

42. Representing that persons being solicited to purchase respondents' land are being asked to take the first step, are reserving the land, are taking an option to buy the land, are not making a final decision, or are not buying the land; or otherwise misrepresenting the legal significance of signing a contract.

43. Representing that prospective purchasers must sign a contract immediately in order to assure purchasing real property in a choice location or in a particular subdivision or community, unless such is the fact; or misrepresenting the number of lots available for

sale at present or in the future in any subdivision, group of interrelated subdivisions, or other area.

44. Failing to clearly and conspicuously disclose, both orally and in writing, to each prospective purchaser of any lot which is located within one-half mile of railroad tracks, the distance of the lot from said railroad tracks.

45. Including in any contract or other document any waiver, limitation or condition on the right of a purchaser to cancel a transaction or receive a refund under any provision of this order, except as such waiver, limitation or condition is by this order expressly allowed.

46. Including in any contract for the sale of land, or in any document shown or provided to purchasers or prospective purchasers of land, whether or not signed by such purchasers or prospective purchasers, language stating expressly or by implication:

(a) That no express or implied representations have been made in connection with the sale of respondents' land, or that any particular representation has not been made in connection therewith;

(b) That the purchaser has had an opportunity to examine or understand any property report, offering statement or similar document required by state or federal law to be made available to him; *provided, however,* that such language may be included when required by the Interstate Land Sales Full Disclosure Act, presently codified at 15 U.S.C. 1701-20 (1970).

47. Making any statement or representation concerning the rights or obligations of respondents or the purchaser which differs in any material respect from the rights or obligations of the parties as stated in the contract.

48. Misrepresenting the right of a purchaser to cancel a transaction or receive a refund under any provision of this order or any applicable statute or regulation.

49. Misrepresenting to any prospective purchaser or purchaser of land the contents or significance of any pleading, finding of fact, conclusion of law, order, decision, opinion, or any other document or written or oral ruling concerning any legal proceeding in a court, before an administrative agency, or in any other forum.

II

It is further ordered:

A. That within two months after this order becomes final respondents forward to all current purchasers of land in Palm Beach Heights the letter attached as Appendix A; *provided, however,* that if changes are necessary to render such letter accurate as of the date of mailing, respondents shall submit such changes to the Commission not less than 45 days prior to the date of mailing. The Commission, within 30 days after its receipt of such changes, shall have the right to reject them in whole or in part, and respondents will then mail such letter with the changes, if any, which were not rejected by the Commission.

B. That within two months after this order becomes final respondents forward to all current purchasers of land in any of the Rotonda subdivisions who purchased their lots prior to June 1, 1978, the letter attached as Appendix B; *provided, however*, that if changes are necessary to render such letter accurate as of the date of mailing, respondents shall submit such changes to the Commission not less than 45 days prior to the date of mailing. The Commission, within 30 days after its receipt of such changes, shall have the right to reject them in whole or in part, and respondents will then mail such letter with the changes, if any, which were not rejected by the Commission.

C. That with respect to all contracts for the purchase of respondents' land other than the Perdido Bay Country Club Estates and Runaway Bay subdivisions entered into prior to the date this order becomes final, respondents or their agents or representatives shall not (i) take legal action, or threaten to take legal action, to recover unpaid balances due under such contracts in the event a purchaser defaults; or (ii) represent to purchasers that they are personally liable to complete the payments under their contracts. In addition, respondents shall obtain and destroy all copies of executed promissory notes other than those in the possession or control of purchasers.

D. (1) That within six months after this order becomes final respondents set aside and designate in the land records of Charlotte County, Florida, a portion of their property on Don Pedro Island, comprised of contiguous land exceeding five acres in size which fronts at least 400 feet on both the Gulf of Mexico and Lemon Bay, as not to be sold but to be retained by respondents in perpetuity for the use of residents of all the Rotonda subdivisions and as not to be further improved except in a manner consistent with such use, and file in the land records of Charlotte County a perpetual easement pursuant to which residents of all the Rotonda subdivisions will be granted access to the entire beach consistent with current state law; and (2) that respondents retain such property in perpetuity for the use of residents of all the Rotonda subdivisions and not improve such land except in a manner consistent with such use; *provided, however,* that nothing herein shall prevent respondents from causing such property to be conveyed to one or more duly constituted Rotonda property owners associations or prevent respondents from reserving an easement over or title to such property for the purpose of assuring access over the property.

E. That for a period of seven years from the date this order becomes final respondents shall continue to provide free ferry service for Rotonda residents to Don Pedro Island, consistent with the ferry service previously provided such residents, and at the conclusion of such period respondents shall convey free and clear title to a ferry or other suitable water vehicle in good working condition, to one or more duly constituted Rotonda property owners associations.

F. That except with the prior authorization of the Commission, respondents, through June 30, 1990:

1. Shall limit the sale and development of land in Charlotte County, Florida, to the following land: the Rotonda subdivisions as platted on January 1, 1977, the land contiguous to the Rotonda subdivisions owned by respondents as of January 1, 1977, the Cape Haze subdivision, and Don Pedro Island; and

2. Shall not sell, in the land comprising the Rotonda subdivisions on January 1, 1977, a greater number of lots, or lots which would contain in the aggregate a greater potential population, than is contained in the plats in effect on January 1, 1977 for the Rotonda subdivisions. For the purposes of this subparagraph, (a) lots sold prior to the date this order becomes final shall be included in determining the number of lots sold or the potential population of the lots sold; and (b) lots returned to inventory due to forfeiture, exchange, or any other reason shall not be considered as sold.

G. 1. That respondent Cape Cave Corporation send copies to the Commission of any reports concerning land development at the Rotonda subdivisions, or the expenditures for or the financing of such land development, which are or may be required to be submitted to the Division of Florida Land Sales and Condominiums, Department of Business Regulation, State of Florida ["Division"], including but not limited to any "Improvement Trust Reports" required to be submitted to the Division pursuant to various Improvement Escrow Agreements to which the Division and Cape Cave Corporation are parties. Cape Cave Corporation shall submit copies of such reports within 15 days of the date said reports are required to be submitted to the Division.

2. Respondent Cape Cave Corporation shall maintain, for a period of 5 years after they are prepared, copies of all audited financial statements not submitted to the Commission pursuant to subparagraph (1) above, and shall make such financial statements

available during normal business hours to the Commission for inspection and copying.

III

It is further ordered:

A. That respondents deliver, by certified mail or in person, a copy of this order to all of their present and future salesmen and other employees, independent brokers, advertising agencies and others who sell or promote the sale of respondents' land or who otherwise have contact with the public on behalf of respondents;

B. That respondents provide each person so described in paragraph (A) above with a form to be returned to respondents, clearly stating that person's intention to conform his or her business practices to the requirements of this order;

C. That respondents inform each person described in paragraph (A) above that respondents shall not use any such person or the services of any such person, unless such person agrees to and does file notice with respondents that he or she will conform his or her business practices to the requirements of this order;

D. That in the event such person will not agree to so file notice with respondents and to conform his or her business practices to the requirements of this order, respondents shall not use such person or the services of such person;

E. That respondents so inform the persons described in paragraph (A) above that respondents are obligated by this order to discontinue dealing with those persons who engage on their own in the acts or practices prohibited by this order;

F. That respondents institute a program of continuing surveillance adequate to reveal whether the sales practices of each of said persons described in paragraph (A) above conform to the requirements of this order; and

G. That respondents discontinue dealing with any person described in paragraph (A) above, revealed by the aforesaid program of surveillance, who repeatedly engages on his own in the acts or practices prohibited by this order; *provided, however,* that in the event remedial action is taken, the sole fact of such dismissal or termination shall not be admissible against respondents in any proceeding brought to recover penalties for alleged violation of any other paragraph of this order.

IV

It is further ordered:

A. That in the event the Interstate Land Sales Full Disclosure Act, presently codified at 15 U.S.C. 1701–20 (1970), or any regulation promulgated pursuant thereto by the Office of Interstate Land Sales Registration of the U.S. Department of Housing and Urban Development, requires an act or practice which is prohibited by any provision of this order, such order prohibition shall be inoperative.

B. That in the event any provision of this order requires an act or practice which is prohibited by the Interstate Land Sales Full Disclosure Act, presently codified at 15 U.S.C. 1701–20 (1970), or any regulation promulgated pursuant thereto by the Office of Interstate Land Sales Registration of the U.S. Department of Housing and Urban Development, such order requirement shall be inoperative.

C. That in the event the Commission promulgates a valid trade regulation rule applicable to respondents' sale of land to consumers which contains provisions setting out the amount or percentage of moneys paid by a purchaser which may be retained by the seller in the event of the purchaser's default, then paragraph 19 of this order shall be deemed modified by said provisions of the trade regulation rule, and said provisions shall be incorporated into this order.

D. That in the event the Commission promulgates a valid trade regulation rule applicable to respondents' sale of land to consumers which contains provisions setting out disclosures to be made in contracts and/or in advertisements and promotional materials, any parts of paragraphs 3 and 4 of this order which are inconsistent with the disclosures set out in said trade regulation rule shall be deemed modified by said provisions of the trade regulation rule, and said provisions shall be incorporated into this order.

E. That in the event the notices required to be sent to purchasers by paragraphs II (A) and (B) of this order are required by law to be approved by another federal agency prior to dissemination, in the event respondents submit such notice or offer to the appropriate federal agency for approval at least 45 days prior to the date it is due to be disseminated under this order and such approval is not granted within 30 days, then the date by which the notice or offer must be disseminated will be extended to 15 days following the date respondents receive notice that such approval has been granted.

F. That this order shall become effective in accordance with standard Federal Trade Commission procedure; *provided, however,* that all written advertising and promotional materials, and form contracts, which must be filed with and accepted for dissemination by state or federal agencies, shall not be subject to the provisions of this order, except for those provisions which prohibit or limit the use of any statement, representation, or misrepresentation, for a period of six months from the date this order becomes final or until said acceptance for dissemination is obtained from all applicable state or federal agencies, whichever occurs first; and *further provided,* that until said six month period expires or said acceptance for dissemination is obtained, whichever occurs first, respondents shall file with the Commission monthly reports detailing respondents' progress toward obtaining the aforementioned acceptance for dissemination by the applicable state or federal agencies.

V

It is further ordered, That respondent corporations shall forthwith distribute a copy of this order to each of their operating divisions engaged in the sale of real property of consumers.

It is further ordered, That respondents herein shall, within 60 days after service upon them of this order, file with the Commission a report in writing setting forth in detail the manner and form in which they have complied with this order.

It is further ordered, That respondents notify the Commission at least 30 days prior to any proposed change in the corporate respondents, such as dissolution, assignment, reorganization, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of this order.

Commissioner Pitofsky did not participate.

APPENDIX A

FEDERAL TRADE COMMISSION

WASHINGTON, D. C. 20580

BUREAU OF CONSUMER
PROTECTION

IMPORTANT NOTICE TO PALM BEACH HEIGHTS LOT BUYERS

The Federal Trade Commission is sending this letter to all Palm Beach Heights lot purchasers. It contains facts you should know about your lot.

Palm Beach Heights is owned by Palm Beach Heights Development and Sales Corporation. Lots in Palm Beach Heights were sold on behalf of the owner by Palm Beach Investment Properties, Inc., a subsidiary of Cavanagh Communities Corporation.

In 1975, the Federal Trade Commission began a lawsuit against Cavanagh Communities Corporation, Palm Beach Investment Properties, Inc., and other subsidiaries of Cavanagh. This letter is part of a Consent Order which has been reached in settlement of that lawsuit.

Please read this letter and think about it carefully.

Your Palm Beach Heights lot.

Under your contract, the owner of Palm Beach Heights is required to put in unpaved (sand or gravel) roads. Many of these roads were required to be completed by December 31, 1975 or December 31, 1976. At the time of your purchase, county permits were not required in order to install the roads. Since that time, however, the county passed an ordinance which prohibits the construction of unpaved roads in subdivisions such as Palm Beach Heights, and therefore no roads have yet been constructed. The owner of Palm Beach Heights has filed a lawsuit in order to get unpaved roads approved for Palm Beach Heights, but has thus far been unsuccessful. If the county wins the lawsuit and if the owner refuses to put in paved roads, there will be no roads in Palm Beach Heights at all. Unless roads are constructed in Palm Beach Heights, your lot will not be usable as a homesite.

It will be difficult to resell your lot.

Even if the roads are put in, it is unlikely that you will be able to resell your lot in the foreseeable future at or near the price you have paid or are paying for it. You should be aware that neither Cavanagh nor Palm Beach Investment Properties will buy back your lot or help you resell it.

Palm Beach Heights is likely to remain undeveloped.

The owner of Palm Beach Heights is not required to put in electric or telephone lines, recreational canals, or any amenities whatever. In addition, the owner is not required to see that your lot has a water supply or a means of sewage disposal. The owner is required only to put in unpaved roads and drainage. Even if unpaved roads are eventually built, the owner does not have to maintain them, and they may become impassable due to erosion unless the property owners themselves decide to provide for maintenance.

Payment for improvements and taxes.

Under your contract, you are required to pay assessments for roads and drainage, taxes on your lot, and interest on both assessments and taxes if the owner has paid these costs on your behalf. You should be aware that you will be required to make a payment of between $500 and $1000 per acre after you complete your regular payments to pay for these additional costs.

The matters discussed in this letter are serious, and require your attention.

If you have any questions about the contents of this letter, write to me. Please do not telephone.

If you have questions about your account or your specific lot call Cavanagh *collect* at (305) 353-1200. An account executive will return your call. Instead of calling, you may wish to write to:

Cavanagh Communities Corporation
444 Brickell Avenue
Miami, Florida

In any letter you should include your name as set forth in your contract, your account number, your current address and telephone number, and the name of the subdivision in which your lot is located.

Sincerely,
Jeffrey Tureck
Attorney

APPENDIX B

IMPORTANT NOTICE TO ROTONDA LOT BUYERS

The Federal Trade Commission is sending this letter to all Rotonda lot buyers. It contains facts you should know about your lot.

In 1975, the Federal Trade Commission brought a lawsuit against Cavanagh Communities Corp., Cape Cave Corp. (the developer of Rotonda) and other Cavanagh subsidiaries. This letter is part of the Consent Order issued when the lawsuit was settled. The Deltona Corporation, which has managed Rotonda since May 1976, was not a party to the lawsuit or the Consent Order.

Please read this letter and think about it carefully. Then decide whether to go on making payments or stop. If you stop, you'll lose your lot and all the money you've paid for it so far.

In order to assist you in making your decision, you should consider all the facts outlined below:

I. LOT VALUE AND RESALE

[The following two paragraphs shall be included in letters to purchasers of lots in Rotonda West other than the Oakland Hills and Pebble Beach segments:]

There is no resale market in Rotonda for lots which have not been developed. If your lot is presently undeveloped, it is unlikely that you would be able to resell it now even at a substantial loss. The extent of community development and population growth in the particular area of Rotonda where your lot is located will determine whether or not you could resell your lot once it is developed. The population growth and community development necessary to enable you to sell your lot at or near the price you paid or are paying for it may not occur for many years.

You should be aware that neither Cavanagh nor The Deltona Corporation will buy back your lot or help you resell it.

[The following two paragraphs shall be included in letters to purchasers of lots in all Rotonda subdivisions other than Rotonda West, except that the words "if at all" at the end of the first paragraph shall be omitted in letters to purchasers of lots in Rotonda Heights, Rotonda Lakes, and Rotonda Shores:]

There is no resale market in Rotonda for lots which have not been developed. Since your lot is presently undeveloped, it is unlikely that you would be able to resell it now even at a substantial loss. After your lot is developed, it is unlikely that you will be able to resell it at or near the price you paid or are paying for it until there is substantial community development and population growth, which may not occur for many years, if at all.

You should be aware that neither Cavanagh nor The Deltona Corporation will buy back your lot or help you resell it.

II. STATUS OF ROTONDA

A. Changes in Plan of Development

The following changes or clarifications in the plans for the development of Rotonda have been announced by Cape Cave.

Except for the modifications described below, Cape Cave plans to complete construction and development of the Rotonda Community consistent with its contractual obligations. However, there is no guarantee that Cape Cave will be able to live up to these obligations. It is important to note that many of the changes discussed in this notice must still be approved by the appropriate governmental agencies. The approval process can be lengthy and its results cannot be assured.

1. *Improvement Schedule* - Cape Cave presently estimates that the improvements in Rotonda Lakes, Rotonda Heights, and certain areas of Rotonda West (Broadmoor, Long Meadow, White Marsh, and Pine Valley) will be finished December 31, 1978, instead of December 31, 1977. Also, it is estimated that Rotonda Springs will be finished by July 31, 1983, instead of August 31, 1982. Cape Cave now plans to complete all other subdivisions on time *except* for about 1400 lots in Rotonda Sands (and about a hundred lots elsewhere) which cannot be developed *at all.* Purchasers of these lots will be notified within 30 days and will be advised of certain exchange rights to lots which can be developed.

2. *Improvement Assessments - Current studies indicate that Cape Cave's original improvement assessment estimates will no longer be accurate in most instances.* As a result, substantially higher assessment charges for many existing lot purchasers will be necessary. [Put in revised assessment figures.]

3. *Golf Courses* - The original design of Rotonda West was based upon construction of seven golf courses, one in each segment of Rotonda West except St. Andrews, by December 31, 1977. The golf course in the Oakland Hills segment of Rotonda West is complete and open to the public for play. However, while Cape Cave is also required by contract to complete the other six courses by that date, Cape Cave is no longer planning to do so. The areas formerly planned as golf courses will instead be landscaped to resemble golf courses, *but will not be playable.* Although Cape Cave has agreed to keep money in escrow to open the other golf courses later, this does not mean these courses will be built. Based on population projections, it does not seem that there will be a need for the second golf course for at least 5 years. The remaining courses are unlikely to be opened for many years, if ever.

B. Flood Prevention Costs

The Rotonda subdivisions, like most of coastal Florida, are located within an area now designated by the U.S. Department of Housing and Urban Development as a 100-year flood plain. That means it is expected that property in the area which is below a certain height may be subject to flooding once in 100 years. The Charlotte County Zoning Regulations now require that new houses shall have the lowest floor of the house built at or above the level of the 100-year flood. Many lots in Rotonda, including all or most lots in Rotonda Springs, Villas, [etc.] are below the 100-year flood level and will not be raised by the developer to such a level. Additional fill dirt or pilings paid for by the lot owner would therefore be required in order to build on these lots. The cost of fill dirt depends on the size of the house and lot and on the number of feet of elevation needed. For average houses and lots, the cost of fill dirt presently ranges from about $400 for one foot of elevation to about $2300 for four feet of elevation. Should you decide to use pilings, the cost is much greater.

C. Various Improvements, Amenities and Facilities

The complaint issued by the Federal Trade Commission also alleged that certain statements had been made regarding other plans for Rotonda which are not dealt with in your contract. The following information deals with those matters:

1. *Waterways* - In order to get permits to develop Rotonda, Cape Cave has had to make significant changes in the Rotonda canal system. Only 26 miles of the original

32-mile canal system are still proposed to be completed. None of the canals will connect with either Coral Creek (the large lake in Rotonda West) or the Gulf of Mexico. Although Deltona may attempt to get permits to connect the canal system to the Gulf, it is unlikely that they will be successful. Finally, you should be aware that the canal system will not be usable for such sports as water skiing.

2. *Don Pedro Island*

(a) While there are no current plans for development, it is anticipated that Don Pedro Island, where the beach for Rotonda is located, may eventually be developed with high-rise condominiums and other structures.

(b) Cape Cave will designate an area of Don Pedro Island, comprising not less than 400 feet of beach frontage, for the perpetual use of Rotonda residents. This area is in addition to the beach frontage along the entire beach which must be maintained as a public area under Florida law.

(c) Access to Don Pedro is presently available free of charge by ferry from Gasparilla Marina, near Rotonda. Cape Cave has agreed to continue free ferry service to Don Pedro Island through 1983, after which the ferry will be donated to a Rotonda property owners association.

3. *Clubhouses* - At one time plans were announced to build a multi-million dollar clubhouse in Oakland Hills. This structure will not be erected. A more modest clubhouse has been constructed at a cost of approximately $300,000. Other clubhouses are planned to be built when additional golf courses are opened, which probably will not occur for many years, if at all.

4. *Power Lines, Curbs and Gutters* - The Oakland Hills segment of Rotonda West will be serviced by underground power and telephone lines. All other power lines throughout Rotonda will be above ground. Oakland Hills will also be the only part of Rotonda to be constructed with curbs and gutters. In the rest of Rotonda, drainage will be provided by grass swales next to the paved roadway system.

5. *Commercial Establishments, Facilities, and Residential Housing* - Cape Cave assumes no responsibility, and has no plans, for development of the central core of Rotonda West. The company also assumes no obligation to establish commercial facilities in any other area of Rotonda or to assure that any existing commercial establishments remain in operation. A number of proposed housing projects and facilities that were previously announced will not be constructed. These include a hotel, garden apartments, and a townhouse complex.

D. Environmental Problems

The development of some areas in Rotonda is subject to the issuance of permits by government agencies. Delays, or rejection of proposed developments, are often encountered in attempting to obtain the necessary permits required for construction to proceed in such areas.

Permits to develop Rotonda ______ have not been applied for at this time from the appropriate government agencies. Since the development of these subdivisions could have an adverse impact on the environment, there is a chance that these permits will be denied. If these permits are denied, Rotonda ______ etc. could not be developed as planned. Therefore, if you continue to make payments you should be aware that there is some degree of risk that the permits will be denied, and your lot may not get developed.

IV. OPTIONS AVAILABLE TO PURCHASERS

There are a number of options available to you at this time which you should review based on the information provided in this notice:

1. You can continue making your payments.

2. You can refuse to make any further payments. According to your contract and the FTC Consent Order you *cannot* be required to pay any more money. If you elect this option, you will lose your land and all the money you have paid. Also, if you purchased your lot as an investment and not for your own use as a homesite, you may be able to declare the money you lost as a tax loss, deductible from your income on federal and state tax returns. It is suggested that you contact your local District Director of the Internal Revenue Service before deciding whether to stop payments, if your decision is based on the possibility of taking a tax loss. Whether your loss is deductible will be based on your specific situation.

3. Under your contract, you may have the right to exchange your lot for a different lot in Rotonda. You may be required to pay more money for this new lot, however.

4. Your contract has a "grace period" under which you can withhold payments without giving up your land for a period of from 60–150 days, depending upon the amount of money you have paid on your contract.

If you have any questions about the contents of this letter, write to me. Please do not telephone.

If you have questions about your account or the development of your specific lot call the Rotonda Customer Affairs Department of Deltona *toll free* at (800) ————. An account executive will return your call. Instead of calling, you may wish to write to:

Rotonda Customer Affairs
P. O. Box 450783
Miami, Florida 33145

In any letter, you should include your name as set forth in your contract, your account number, your current address and telephone number, and the name of the Rotonda subdivision in which your lot is located.

Sincerely,

Jeffrey Tureck
Attorney

IN THE MATTER OF

AMWAY CORPORATION, INC., ET AL.

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9023. Complaint, March 25, 1975 — Final Order, May 8, 1979

This order, among other things, requires two Michigan corporations engaged in the door-to-door marketing of various household products, and two corporate officers, to cease allocating customers among their distributors; fixing wholesale and retail prices for their products; taking retaliatory action against recalcitrants; and disseminating price-listing data which fail to advise that price adherence is not obligatory. Respondents are additionally prohibited from misrepresenting potential earnings and other relevants to prospective distributors.

Appearances

For the Commission: *Joseph S. Brownman, D. Stuart Cameron, Mary Lou Steptoe, B. Milele Archibald* and *Michael Goldenberg.*

For the respondents: *Lee Loevinger, Philip C. Larson* and *Robert J. Kenney, Jr., Hogan & Hartson,* Washington, D.C. and *John E. Stephen,* Ada, Mich.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act (15 U.S.C. 41, *et seq.*) and by virtue of the authority vested in it by said Act, the Federal Trade Commission having reason to believe that the parties listed in the caption hereof and more particularly described and referred to hereinafter as respondents, have violated the provisions of Section 5 of the Federal Trade Commission Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the interest of the public, hereby issues its complaint, stating its charges as follows:

PARAGRAPH 1. Respondent Amway Corporation, Inc. is a corporation organized on or about September 6, 1949, under the name Ja-Ri Corporation, Inc. Its name was formally changed to Amway Corporation in November 1963. On or about January 1, 1964, Amway Sales Corporation, Amway Services Corporation and Amway Manufacturing Corporation, all of which were Michigan corporations, were merged into Amway Corporation, Inc. Respondent corporation maintains its home office and principal place of business at 7575 East Fulton Rd., Ada, Michigan. [2]

PAR. 2. Respondent Amway Distributors Association of the United

States is an association of Amway distributors and dealers, which maintains its home office and principal place of business at 7575 East Fulton Rd., Ada, Michigan. Among the functions and duties of the Amway Distributors Association are to make recommendations to respondent corporation with respect to the standing, termination or suspension of individual distributors or dealers, and to recommend changes or other action on various restrictions upon distributors or dealers.

PAR. 3. Respondent Jay Van Andel is Chairman of the Board of Directors of respondent corporation, and was one of its founders. Together with others, respondent Van Andel instituted the Amway marketing plan and distribution policies, and has been and continues to be responsible for establishing, supervising, directing and controlling the business activities and practices of corporate respondent. Mr. Van Andel's office address is the same as that of respondent corporation.

PAR. 4. Respondent Richard M. DeVos is President of respondent corporation, and was one of its founders. Together with others, respondent DeVos instituted the Amway marketing plan and distribution policies, and has been and continues to be responsible for establishing, supervising, directing and controlling the business activities and practices of corporate respondent. Mr. DeVos' office address is the same as that of respondent corporation.

PAR. 5. Respondent corporation is engaged in the manufacture, distribution, offering for sale and sale of more than 150 kinds of home-care, car-care and personal-care products, as well as vitamins and food supplements, under its own labels and trademarks, to distributors and dealers located throughout the United States. In addition, respondent corporation sells over 300 products manufactured by and bearing the name and label of other manufacturers. These products are of a wide variety including clothing, household appliances, furnishings, tools, luggage, watches, cameras and other items. Sales of products by the respondent corporation is more than $150,000,000 at retail levels, and over 200,000 persons are actively engaged in the resale of Amway products throughout the United States. [3]

PAR. 6. In the course and conduct of its business of manufacturing and distributing its products, respondent corporation ships or causes such products to be shipped from the state in which they are manufactured and warehoused to distributors or dealers located in various other States throughout the United States. These distributors in turn resell to other distributors, dealers or to members of the general public. There is now and has been for several years last past a constant, substantial, and increasing flow of such products in or

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affecting "commerce" as that term is defined in the Federal Trade Commission Act.

PAR. 7. Except to the extent that actual and potential competition has been lessened, hampered, restricted and restrained by reason of the practices hereinafter alleged, respondent corporation's distributors and dealers, in the course and conduct of their business of distributing, offering for sale, and selling their products are in substantial actual competition or potential competition in commerce with one another, and corporate respondent is in substantial actual or potential competition in commerce with other persons or firms engaged in the manufacture, sale and distribution of similar merchandise.

PAR. 8. Respondents have formulated a distribution system which has been published in various manuals, bulletins, pamphlets and other literature and material. To effectuate and carry out the policies of this distribution system, corporate respondent has entered into contracts, agreements, combinations or common understandings with its distributors and dealers; and has adopted, placed into effect, enforced and carried out, by various methods and means, said distribution system, which hinders, frustrates, restrains, suppresses and eliminates competition in the offering for sale, distribution and sale of its various products.

PAR. 9. Distributors and dealers of respondent corporation are independent contractors who sell or attempt to sell at retail to members of the consuming public, and at wholesale to other distributors and dealers recruited and/or sponsored into their respective sales organizations. Except for "Direct Distributors," distributors or dealers generally purchase their product needs directly from their sponsors. [4]

Distributors buying directly from respondent corporation are denoted "Direct Distributors," of which there are approximately fifteen hundred (1500) throughout the United States. Other distributors or dealers may purchase directly from Amway Corporation after meeting certain conditions.

In concert and combination with their network of distributors and dealers, respondents police, enforce and carry out the various rules, regulations and policies, including those alleged hereinafter as unfair methods of competition and unfair or deceptive acts or practices.

COUNT I

Paragraphs One through Nine are incorporated by reference herein as if fully set forth verbatim.

PAR. 10. The acts, practices and methods of competition engaged in, followed, pursued or adopted by respondents, and the combination, conspiracy, agreement or common understanding entered into or reached between and among the respondents, respondent corporation's distributors or dealers, or others not parties hereto tend to, and do, fix, maintain, control or tamper with the resale prices at which respondent corporation's products are or may be sold.

PAR. 11. For example, distributors and dealers have entered into contracts, agreements, combinations or understandings with respondents, or have been and continue to be required and coerced by respondents to sell to other distributors or dealers at other wholesale levels of distribution at the same prices which they paid for their products from other distributors or dealers or from respondent Amway Corporation. Distributors or dealers must thereafter rely upon the implementation of and adherence to respondents' purchase volume refund schedule for wholesale profits.

Under this purchase volume refund plan, refunds are paid by respondent Amway Corporation to its direct buying "Direct Distributors" on a monthly basis at the rate of 25% of the monthly dollar volume of purchases figured at the retail price. These sponsoring distributors, in turn, pay rebates to their wholesale customers of from 0 to 25%, based upon their own monthly dollar volume of purchases, and so on, to all wholesale levels of distribution. [5]

PAR. 12. By way of further example, distributors and dealers have also agreed to sell to church, service, civic or charitable selling organizations at specified prices, and to in turn request these organizations to adhere to these same retail prices when selling to the ultimate consumer. Thereafter the distributor or dealer will pay the selling organization a sum of money which will become its gross income on the aforesaid sales.

Said acts, practices and methods of competition, and the adverse competitive effects resulting therefrom, constitute unreasonable restraints of trade and unfair methods of competition in commerce within the intent and meaning of Section 5 of the Federal Trade Commission Act, as amended.

COUNT II

Paragraphs One through Nine are incorporated by reference herein as if fully set forth verbatim.

PAR. 13. The acts, practices and methods of competition engaged in, followed, pursued or adopted by respondents, and the combination, conspiracy, agreements or common understandings entered into or reached between and among the respondents, respondent corporation's distributors or dealers, or others not parties hereto tend to, and do, restrict the customers to whom respondent corporation's distributors or dealers may resell their products; restrict distributors and dealers as to the source of their product needs; restrict the retail outlets through which distributors and dealers may resell their products; and allocate retail customers between and among the various distributors or dealers.

PAR. 14. Distributors and dealers have entered into contracts, agreements, combinations or understandings with respondents, or have been and continue to be required and coerced by respondents to adhere to practices whereby absent prior approval to the contrary, purchases of product needs must be made either directly from respondent corporation or from the distributor or dealer who recruited and/or [6] sponsored the would-be purchasing distributor or dealer. Distributors and dealers may not resell their products at wholesale except to those other distributors or dealers they had recruited and/or sponsored, and who are recognized as such by respondents. Distributors or dealers who drop out of the program are replaced in the chain of distribution by other distributors or dealers to whom the former had previously been selling.

PAR. 15. Distributors and dealers have also entered into contracts, agreements, combinations or understandings with respondents, or have been and continue to be required and coerced by respondents to refrain from selling from or through any business office, retail store, military store, ship's store, service station, barber shop, beauty salon, show booth, fair or the like, and to refrain from selling to proprietors of such establishments for resale at the retail level.

PAR. 16. Distributors and dealers have also entered into contracts, agreements, combinations or understandings with respondents, or have been required and coerced by respondents to refrain from soliciting the business of retail customers and commercial accounts of other distributors or dealers.

Said acts, practices and methods of competition, and the adverse competitive effects resulting therefrom, constitute unreasonable restraints of trade and unfair methods of competition in commerce within the intent and meaning of Section 5 of the Federal Trade Commission Act, as amended.

COUNT III

Paragraphs One through Nine are incorporated by reference herein as if fully set forth verbatim.

PAR. 17. The acts, practices and methods of competition engaged in, followed, pursued or adopted by respondents, and the combination, conspiracy, agreements or common understandings entered into or reached between and among the respondents, respondent corporation's distributors or dealers, or others not parties hereto tend to, and do, restrict the advertising and promotional activities in which distributors and dealers may or would otherwise engage. [7]

PAR. 18. Distributors and dealers have entered into contracts, agreements, combinations or understandings with respondents, or have been required and coerced by respondents to refrain from engaging in or limiting advertising activities as follows:

1. Distributors and dealers may not display literature or merchandise in the locations from which retail sales activities are prohibited.
2. "Direct Distributors" only may display the "Amway" tradename, tradmarks or logos on the exterior of their places of business; provided that in addition thereto the place of business is a commercial type building, the place of business is an exclusively Amway business, no displays appear in any show windows, a view from the outside looking in is obscured, and "Wholesale Only" must appear on the door leading in.
3. Distributors and dealers other than "Direct Distributors" must obtain the permission of the Direct Distributors from whose chain of distribution they purchase merchandise before the Amway logo may be displayed on business vehicles.
4. "Direct Distributors," with prior permission, may advertise in the "white pages" of the telephone directory under the "Amway" tradename, whereas other distributors or dealers may not.
5. Distributors and dealers may not utilize display ads in "yellow pages" telephone directories wherein it is indicated that the distributor or dealer deals in Amway merchandise.
6. Distributors and dealers may not set up displays at fairs, home shows or other special events unless they do so in concert, and under the direction of a "Direct Distributor." [8]
7. "Direct Distributors" only may utilize roadside advertising.
8. Distributors and dealers other than "Direct Distributors" may not advertise in newspapers, magazines or on the radio or television.
9. Distributors and dealers may only place recruiting ads which do not mention the name "Amway."
10. Distributors and dealers may not advertise specific Amway products in the media.

Said acts, practices and methods of competition, and the adverse competitive effects resulting therefrom, constitute unreasonable restraints of trade and unfair methods of competition in commerce within the intent and meaning of Section 5 of the Federal Trade Commission Act, as amended.

COUNT IV

Paragraphs One through Nine are incorporated by reference herein as if fully set forth verbatim.

PAR. 19. By and through the use of written or oral representations, respondents or their representatives represent and have represented, directly or by implication that:

1. Substantial income or profit as a result of wholesale or retail sales activities from "multiplication," "duplication" or geometrical increases in the number of distributors at lower functional levels of distribution is likely.

2. Substantial income or profit as a result of wholesale or retail sales activities from unlimited recruiting activities or endless chain recruiting activities is likely. [9]

PAR. 20. In truth and in fact the distributors and dealers are not long likely to recruit other distributors in multiplication, duplication, geometrically increasing, unlimited or endless chain fashion, or to profit from sales to other distributors at lower functional levels in geometrically increasing, unlimited, or endless chain fashion because:

(a) The participants may be, and in a substantial number of instances will be, unable to find additional participants, by the time they enter respondents' marketing program. As to each of the individual participants, recruitment of additional participants must of necessity ultimately collapse when the number of persons theretofore recruited has so saturated the area with distributors or dealers as to render it virtually impossible to recruit others.

(b) Profits resulting from respondents' recruitment program must of necessity ultimately collapse when the number of potentially available persons who can be recruited to serve a particular area is exhausted. The greater the number of distributors or dealers previously recruited, the lower the chances of a profitable distributorship or dealership operation.

(c) Regardless of the number of distributors or dealers previously recruited to serve in a particular market area, profits and therefore recruitment must of necessity ultimately collapse when distributors or dealers at lower functional levels of distribution are unable to operate their wholesale businesses at a profit by selling to lower functional levels at prices greater than paid for. The greater the number of levels of distribution, the more inefficient the distribution system becomes, and the less profitable it is likely to be at the lower levels. [10]

For the foregoing reasons and others, respondents' representations that substantial income or profit may be predicated through multiplication, duplication, and geometrical, unlimited or endless chain increases in the number of distributors or dealers recruited, either at the same or lower functional levels of distribution, in connection with the manufacture, sale and distribution of their merchandise, was and is false, misleading and deceptive, and was and is an unfair method of competition and an unfair act and practice within the intent and meaning of Section 5 of the Federal Trade Commission Act, as amended.

COUNT V

Paragraphs One through Nine and Paragraphs Nineteen and Twenty are incorporated by reference herein as if fully set forth verbatim.

PAR. 21. In the course and conduct of their business, and for the purpose of inducing the purchase of their products and the participation of persons as dealers or distributors of respondents' products, the respondents and their representatives or agents have made and are continuing to make oral and written statements and representations to distributors, dealers and prospective participants regarding the sale of their merchandise, the profitability of a dealership or distributorship and the recruitment of still additional participants. Typical and illustrative of said statements and representations, but not all inclusive thereof, are the following (with emphasis omitted):

1. Sponsoring is profitable, regardless of whether you do it on a limited basis as a part-time distributor, or "all-out" as a full-time distributor.

2. Sponsoring is easy! Recruiting new Amway Distributors is not difficult, just as selling Amway products is not difficult. . . .When you have learned to sponsor one, then you simply repeat the process and sponsor two. . . .From that point on, it is just simple multiplication!

3. . . .[T]here is no known limit to how big your business can grow when you sponsor other distributors, who in turn sell products and sponsor still other distributors.

4. With the proven Amway Opportunity success will be yours. . .act now. . . .

5. To build a big business you, plus your 10 distributors-each sponsoring 4 people (total 51 distributors) with everyone selling one hour per day you will earn. . .your total monthly profit $1,368.00. Excellent income for one hour per day. [11]

6. To build a larger business. . .you simply sponsor 10 distributors who work. . .one hour per day. . .You will earn. . .Your total monthly profit . . .$264.00. Great income for one hour per day.

7. By working just one hour per day and making 2 average sales of $4.00 PV each, . . . your total monthly profit . . . .$52.80. Good extra income for one hour per day."

8. How much can I earn? As much as you desire.

9. Amway six year plan for financial independence. Step 1 - become a direct distributor. . . Step 2 - develop one direct distributor per year. . . Annual income after 6 years $24,300.00.

10. Assuming that you become a Direct Distributor within a year's time and that you develop a Direct Distributor each year for the next five years, at the end of six years you can be earning in Direct Distributor bonuses $225 x 5, or a total of $1,125 a month. . . .The $1,069 a month which you receive on your personal group and the 3% refund bonuses of $1,125 on the 5 Direct Distributors whom you personally sponsor will amount to $2,194 a month or a total of $26,328 a year. This is gross income for managing a business of your own. This can be your six-year plan for financial independence.

11. You can realize the achievement of your dreams through the Amway Opportunity. The Amway Opportunity is broad enough for you to achieve whatever your goal is.

12. An Amway pattern for success. . .duplicate yourself. You sponsor 1 distributor each month . . . each of your personally sponsored distributors sponsor 1 distributor each month - up to 6 . . . . at the end of one year. . . . Your personal group would consist of 64 distributors.

13. To build a still bigger business. . . .You, plus your 6 distributors each sponsoring 4 people (total 31 distributors) with everyone selling $5.00 PV per day. . .you will earn. . .your total monthly income. . . . $408. Excellent income for only a few hours per day.

14. With Amway, you start earning money right away with no large inventory investment.

15. The market potential for Amway products is spectacular.

16. Let's say that six of your personally sponsored distributors sponsor four distributors each, and that everyone makes a sale a day. . . . [12]

17. Let's say you have sponsored six distributors. . . . Your distributor organization can look like this:

Your Sponsor
1
You $200 (Retailing)
1
A $300
B $100
C $150
D $50
E $200
F $100

Your total group PV $1,100.00
Total monthly gross income $157.50

As your business continues to grow and as you train and motivate your personally sponsored distributors to retail and to duplicate themselves by sponsoring new distributors, here is how your total PV and income can increase:

Your Sponsor
1
You $200 (Retailing)
1
Dist A and his group $600
Dist B and his group $300
Dist C and his group $200
Dist D and his group $250
Dist E and his group $300
Dist F and his group $400

Your total group PV $2,250.00
Total monthly gross income: $270.00

At this point, your business has started to bring you good returns. Although you should have sponsored additional distributors in the meantime, for the purposes of simplication, we will show only six distributors personally sponsored by you. Your part-time business can expand rapidly from this point onward.

. . .Your income picture for the month can now look like this:

Your Sponsor
1
You $200 (Retailing)
1
Dist A and his group $1,000
Dist B and his group $1,500
Dist C and his group $800
Dist D and his group $500
Dist E and his group $300
Dist F and his group $800

Your total group PV $5,100.00
Total monthly gross income $594.00

[13] 18. The income picture! Let's take a look at your income picture for the month. . . . Immediate income on your personal sales of $200. . . . $60. Income on refund:. . . . $114. Total earnings $174.

If you save $174 a month for six months, you'd have a total of $1,044 toward a Carribean or a South Seas vacation. . . . So for example, five of your distributors sponsor four distributors who each sell $200 for the month. Now the total of your group has grown to 26, and your monthly purchase volume is $5,200. . . . However, your earnings picture for the month can now look like this: Immediate income on your personal sales $60. Refund income . . . $492. Total earnings $552. Thus, you now have an attractive part-time income, and yet this is just the beginning.

PAR. 22. By and through the use of the above quoted statements and representations, as well as other oral and written statements and representations as found in various promotional materials not expressly set out herein, respondents and their representatives or agents represent, and have represented, directly or by implication, to distributors, dealers and prospective participants, that:

1. It is easy for distributors or dealers to recruit and/or retain

persons to participate in the program as distributors, dealers or sales personnel.

2. Distributors or dealers in the program can anticipate receiving or will receive substantial profits or earnings.

PAR. 23. In truth and in fact:

1. It is not as easy as respondents represent for distributors or dealers to recruit and/or retain as distributors, dealers or sales personnel persons who will participate in the sales program.

2. Distributors or dealers in the sales program do not receive nor are likely to receive the substantial profits or earnings that respondents represent that they will receive or are likely to receive. [14]

PAR. 24. The following statements constitute material facts with respect to the making of claims or representations regarding the potential for recruitment of prospective distributors or dealers and/or the profitability of a distributorship or dealership:

1. There is a substantial turnover or dropout rate of distributors, dealers, wholesale and retail sales personnel, and a constant recruitment effort must be made simply to maintain a constant number of sub-distributors, sub-dealers, or sales personnel.

2. There are substantial business expenses associated with an active Amway distributorship or dealership.

PAR. 25. The statements and representations contained in Paragraph Twenty-One, along with other statements and representations not expressly referred to therein, contain claims regarding the potential for recruitment of prospective distributors, dealers or sales personnel and the profitability of a distributorship or dealership; but fail to disclose the material facts set forth in Paragraph Twenty-Four.

The dissemination by respondents of the aforesaid statements and representations, and others, has had, and continues to have, the capacity and tendency to mislead distributors, dealers and prospective participants into the erroneous and mistaken belief that:

1. There is no substantial turnover of distributors, dealers or sales personnel.

2. The turnover of distributors, dealers or sales personnel is not as substantial as they would otherwise have been led to believe.

3. There are no substantial business expenses incurred by distributors or dealers.

4. The business expenses of distributors or dealers are not as substantial as they would otherwise have been led to believe. [15]

PAR. 26. For all of the foregoing reasons, and others, respondents' statements and representations as set forth in Paragraph Twenty-One, as well as others not expressly referred to therein, in connection with the manufacture, sale and distribution of their merchandise, are false, misleading and deceptive, and were and are unfair methods of competition and unfair or deceptive acts or practices within the intent and meaning of Section 5 of the Federal Trade Commission Act, as amended.

INITIAL DECISION BY JAMES P. TIMONY, ADMINISTRATIVE LAW JUDGE

JUNE 23, 1978

PRELIMINARY STATEMENT

By a Federal Trade Commission complaint issued on March 25, 1975, respondents Amway Corporation ("Amway"), Amway Distributors Association of the United States ("ADA"), Jay Van Andel and Richard M. DeVos are charged in five counts with violations of Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45. [2]

Respondent Amway is a corporation organized less than twenty years ago by respondents Van Andel and DeVos. Amway manufactures, distributes and sells with its own trademarks over 150 products, including primarily cleaning and personal care products, and food supplements. While Amway started with soap and other cleaning products, it now sells a wide variety of low cost consumer products, including catalog sales of over 300 products manufactured by and bearing the names of other manufacturers, such as clothing, household appliances, furnishings, tools, luggage, watches and cameras. Amway sells such products through more than 300,000 independent distributors throughout the country. These distributors engage in direct, house-to-house sales to consumers, with total sales amounting to over $200 million in fiscal 1976. The distributors also seek new distributors to build a sales organization. As an incentive to the distributors' sales, Amway offers, *inter alia,* volume discounts based on the total sales of a distributor's sales organization, ranging from 3% on monthly sales over $100 to 25% on sales of about $8,500 and over. Once the distributors reach the top discount bracket, they become "Direct Distributors," receiving such benefits as dealing directly with Amway (rather than through the distributors which sponsored them), and voting membership in the distributors' association, ADA.

The ADA is an association of about 2,500 Amway Direct Distributors, acting as a consultant to Amway on proposed changes in basic sales policies of Amway and as a board of arbitration in disputes between and among distributors and as an appeal board with respect to action by Amway which may affect the rights of distributors.

Amway has a distribution plan published in various manuals, bulletins, pamphlets and other literature and material. This plan, known as the Amway Sales and Marketing Plan, imposes certain limitations upon the distributors' resale of products purchased from Amway and upon the method of recruiting new distributors. The complaint in this case attacks these limitations. Count I of the complaint alleges that respondents engage in resale price maintenance. [3] Count II alleges that respondents allocate customers among distributors and restrict the distributors' source of supply as well as the retail outlets through which they may resell. Count III alleges that respondents restrict the distributors' advertising. Count IV alleges that respondents misrepresent that substantial income may be obtained from geometrical increases in the number of distributors in the chain recruiting operation of the Amway distribution plan. Count V alleges that respondents misrepresent the profitability of a distributorship and the potential for recruiting new distributors and fail to disclose the substantial business expense involved and the high turnover of distributors.

By an answer filed on August 28, 1975, respondents admitted in part and denied in part the various allegations of the complaint. Respondents moved to dismiss the complaint on the grounds that: (1) evidence was improperly obtained by the staff during the course of the pre-complaint investigation, and (2) respondents were not afforded an opportunity to negotiate a settlement prior to the issuance of the complaint. The motion was certified to the Commission by an order dated September 16, 1975; the motion was denied. By an order dated April 12, 1976, I was substituted as administrative law judge because of the heavy workload of the former administrative law judge. An active motion practice ensued, with some thirty contested pretrail orders being issued on a number of procedural question.[1] [4]

Discovery was extensive, involving depositions, interrogatories, requests for admission, and pretrial subpoenas. Counsel filed lists of

[1] Many of respondents' allegations of procedural misconduct were repeated by respondents' counsel on the first day of the trial and are the subject of an additional order, recently entered herein, denying respondents' motion to dismiss.

witnesses and narrative statements of their proposed testimony and exchanged documents to be offered in evidence. The parties filed written statements of relevancy and opposition concerning the offer of hundreds of proposed Commission exhibits. Complaint counsel filed an extensive pretrial statement and proposed findings. The parties filed pretrial briefs.

Hearings started May 16, 1977. The case-in-chief ended on June 7, 1977. The defense started June 28, 1977, and concluded on July 29, 1977. Complaint counsel had a rebuttal case on October 4, 1977. About 150 witnesses testified and the record consists of almost seven thousand pages of transcript and over one thousand exhibits.

Since the last witness testified, the parties have resumed the motion practice, with about thirty additional post-trial contested motions. One of the contested issues involved twenty-three tape recordings received as exhibits during the trial on condition that transcripts be prepared and offered as exhibits. The parties were long at issue over the content of the transcripts of the tapes. The transcripts, when completed, made a pile "two or three feet high." Six full transcripts and seventeen partial transcripts of the tape recordings eventually were offered and received as exhibits.[2] [5]

The post-trial briefs and proposed findings amounted to about 1600 pages. Oral argument was heard on June 6, 1978.

The findings of fact include references to the principal supporting evidence in the record. Such references are intended to serve as convenient guides to the testimony and exhibits supporting the findings of fact, but do not necessarily represent complete summaries of the evidence considered in arriving at such findings. The following abbreviations have been used:

CX - Commission's Exhibit, followed by number of exhibit being referenced.

RX - Respondents' Exhibit, followed by number of exhibit being referenced.

Tr. - Transcript, preceded by the name of the witness, followed by the page number.

CPF - Proposed Finding submitted by Complaint Counsel.

CB - Complaint Counsel's Brief.

CRB - Complaint Counsel's Reply Brief.

RPF - Respondents' Proposed Findings.

[2] Another reason for the delay in closing the record involved the condition of the record. Numerous exhibits were lost or misplaced. At least sixty exhibits had to be replaced with substitutes. The transcript of testimony had numerous errors. Almost all of the changes were stipulated by the parties. The reporter is submitting corrected pages of the transcript during the time that this decision is being prepared, too late for reference herein. Eleven orders were entered concerning this subject, *e.g.*, orders dated March 16, 1978, and June 15, 1978 (denying motion to dismiss of June 6, 1978).

RB - Respondents' Brief. [6]

Findings of Fact

Respondents

1. Respondent Amway Corporation (Amway) is a corporation organized and existing under the laws of the State of Michigan, with its home office and principal place of business at 7575 East Fulton Rd., Ada, Michigan. (Answer, p. 5)

2. Amway currently manufactures and sells more than 150 kinds of home care, car care and personal care products, as well as vitamins and food supplements, all of which are sold under its own labels and trademarks. (Answer, p. 4)

3. The products which Amway sells to its distributors may be grouped into seven major categories as follows: home care and cleaning products; personal care products (such as cosmetics); food supplements; cookware and cutlery; commercial and agricultural products; catalog sales (a wide variety of products); and safety products (such as smoke detectors and fire extinguishers). Soap and detergents account for 41.2% of Amway's 1974 sales; polishes and sanitation goods 20%; and toilet preparations 6.5%. (RX 405)

4. Through its Personal Shoppers Catalog, Amway sells over 300 products manufactured by and bearing the name of other manufacturers. These products include clothes, household appliances, furnishings, tools, luggage, watches, and cameras. (CX 640)

5. Amway distributes its products in the United States through direct selling by authorized independent distributors, which in 1977 numbered approximately 360,000. (RX 383) [7]

6. Amway's dollar volume in sales to distributors in fiscal 1976 was approximately $169 million in the United States and $205 million worldwide. (RX 448; RX 431; Halliday, Tr. 6103, 6105-16)

7. Respondents Jay Van Andel and Richard M. DeVos are co-founders and, together with their wives, are principal owners of Amway. (Van Andel, Tr. 1672, 1781)

8. Mr. Van Andel is Chairman of the Board of Amway. (Van Andel, Tr. 1671)

9. Mr. DeVos is President of Amway. (Complaint, ¶4; Answer, p. 4)

10. Amway's Board of Directors consists of Mr. Van Andel, Mr. DeVos, and William J. Halliday, Jr. (Van Andel, Tr. 1781-82)

11. Respondent Amway Distributors Association of the United States (ADA) is a trade association of Amway distributors organized and existing as a non-profit corporation under Michigan Law.

(Halliday, Tr. 6091-92, 6171-73) ADA maintains its home office and principal place of business at 7575 East Fulton Road, Ada, Michigan. (Complaint, ¶2; Answer)

12. Each new Amway distributor may choose to become a member of the ADA. (Halliday, Tr. 6195-96)

13. An Amway distributor who, through sales volume and other requirements, becomes a "Direct Distributor" may qualify as a voting member of the ADA. (Halliday, Tr. 6196-97) [8]

14. There currently are about 2500 voting members of the ADA. (Halliday, Tr. 6555-56)

15. Voting members of the ADA elect nine members of the eleven-member ADA Board of Directors and Amway appoints two members. Mr. Van Andel and Mr. DeVos represent Amway on the Board. (Halliday Tr. 6194)

16. The ADA Board performs three principal functions: (a) it acts as a representative of the distributor association; (b) it acts as an advisory board to Amway; and (c) it acts as an arbitration board in disputes between distributors or between Amway and a distributor. (Halliday, Tr. 6175-83)

Organization History

17. Mr. Van Andel and Mr. DeVos have been involved in direct selling since 1949, beginning as distributors of Nutrilite food supplements, through a corporation they organized for this purpose—the Ja-Ri Corporation. (Van Andel, Tr. 1672-73, 1676, 1908-10)

18. Direct selling is the distribution of products and related services to consumers in their homes through person-to-person selling. (Van Andel, Tr. 1691-92; Granfield, Tr. 2917-18)

19. In 1959, Mr. Van Andel and Mr. DeVos and other distributors had trouble with their suppliers of food supplements, Nutrilite Products Company, Inc., and Mytinger & Castleberry, Inc. A small group of distributors was appointed, with Mr. Van Andel as the chairman, to try to work out an arrangement with the suppliers. The negotiations culminated in an offer by one of the suppliers to Mr. Van Andel to become president of the company. Mr. Van Andel and Mr. DeVos concluded that the inherent problems were with the people who owned those companies and that those problems would continue regardless of who managed them. Mr. Van Andel refused the offer. (Van Andel, Tr. 1672-73) [9]

20. Mr. Van Andel and Mr. DeVos decided that their suppliers were in great danger of collapsing and that they should go into the business themselves, producing their own products and selling them through the Ja-Ri sales organization which had more than 2000

distributors as members. (Van Andel, Tr. 1674; 1679; Hansen, Tr. 3302; CX 904)

21. Mr. Van Andel and Mr. DeVos then put together an organization of distributors called the American Way Association, the name of which was later changed to the Amway Distributors Association. The primary purpose of this organization was to allow Mr. Van Andel and Mr. DeVos to communicate with their Nutrilite distributors in the Ja-Ri organization and to hold the business together until Mr. Van Andel and Mr. DeVos could develop their own manufacturing operation. (Van Andel, Tr. 1674–75)

22. Mr. Van Andel and Mr. DeVos had to be very careful in changing their distributor organization, with its allegiance to Nutrilite food supplement products. Since the distributors were independent, they might quit. It was therefore necessary for Mr. Van Andel and Mr. DeVos to have these distributors concur in their plans to set up a product distribution and manufacturing operation; and they discussed the type of products they intended to produce with the distributors' association. (Van Andel, Tr. 1674–76) Many of the distributors in the organization of Mr. Van Andel and Mr. DeVos joined the American Way Association, and began distributing products sold to them by Amway as well as Nutrilite products. In 1972, Amway acquired 51% of Nutrilite. (Van Andel, Tr. 1679–80, 1684–85)

23. Mr. Van Andel and Mr. DeVos decided to look for products which were readily consumable, relatively low-priced, different from those found in retail stores, and which would lead to repeat sales. They chose soap and detergents because they felt it would be the easiest market to train distributors to sell in. With that type of product, it is a matter of which one to use rather than whether to use it at all. (Halliday, Tr. 6541; Van Andel, Tr. 1680–81) [10]

24. At about the same time that the American Way Association was formed, Mr. Van Andel and Mr. DeVos began distributing through the Ja-Ri organization a liquid detergent called "Frisk" which they renamed "LOC" (liquid organic compound) and which is still one of the principal Amway products. This product was manufactured by Eckle Company, a small supplier in Detroit, Michigan, and it was one of the only biodegradable liquid detergents available at that time. Mr. Van Andel and Mr. DeVos, through Ja-Ri Corporation, acquired the company, moved the assets to Ada, Michigan, and changed its name to Amway Manufacturing Company. A few months later they introduced SA8, a biodegradable powder detergent. (Van Andel, Tr. 1673–78; Halliday, Tr. 6153, 6541)

25. In November 1959, Mr. Van Andel and Mr. DeVos organized

Amway Sales Corporation and Amway Services Corporation. (Van Andel, Tr. 1677) In November 1963 the name of Ja-Ri Corporation, Inc., was changed to Amway Corporation; and on January 1, 1964, Amway Sales Corporation, Amway Service Corporation, and Amway Manufacturing Corporation were merged into Amway. (Answer, p. 3)

Amway Distribution System

Amway Distributors

26. The Amway Sales and Marketing Plan is designed to move products manufactured by or for Amway through a network of distributors to retail customers. (Halliday, Tr. 6198) Amway imposes several restraints upon distributors as part of this system. The restraints, which are the subject of this litigation, are found in Amway's "Code of Ethics and Rules of Conduct." (RX 331, pp. 13-B through 25-B) The Amway system of recruiting, sponsoring and selling basically is the same as the Nutrilite system which began operating in 1946. (Van Andel, Tr. 1702, 1905-08) [11]

27. The Amway Sales and Marketing plan involves person-to-person retail selling. Amway distributors are urged to sell at retail to persons they know or are referred to, rather than going from door-to-door. (Van Andel, Tr. 1757-58)

28. In the Amway Sales and Marketing Plan, products are sold by Amway distributors, all of whom are independent contractors. (Halliday, Tr. 6261-62)

29. All new Amway distributors enter the business with the same rights and obligations. (Halliday, Tr. 6208; Lemier, Tr. 210-11)

30. Each Amway distributor has the right to sell Amway products to consumers and to sponsor new Amway distributors and to sell products to his sponsored distributors. (Van Andel, Tr. 1708)

31. Any Amway distributor may become a "Direct Distributor" by qualifying on the basis of sales volume. The principal requirement for qualification as a Direct Distributor is that the distributor must have a sales volume of about $8500 per month. (RX 331, p. 8-D

32. Amway sells its products to Direct Distributors, who sel Amway products to consumers and to their sponsored distributoı for resale. (S. Bryant, Tr. 4033-34) Other distributors normally bı from their sponsor. (RX 331, p. 1-E) Those distributors ("Warehou Order Distributors"), living more than 25 miles from their source supply or doing a large volume, are authorized to buy directly fr Amway. (RX 331, p. 1-E) [12]

33. In order to become a duly authorized Amway distributo person must (a) be sponsored by an Amway distributor, and (b)

an application with Amway for the right to sell Amway products. (Van Andel, Tr. 1696–97; RX 331, p. 14–B)

34. A new Amway distributor is not required to buy inventory. The distributor need only buy a $15.60 "Sales Kit" containing product information and sales aids and literature. (RX 331, p. 15–B; Halliday, Tr. 6615)

35. A new distributor may also purchase an optional "Product Kit" for $25.65, containing sample Amway products for demonstration use. (Halliday, Tr. 6126, 6588; RX 433)

36. Neither Amway nor sponsoring distributors make a profit on the Sales Kits. (Van Andel, Tr. 1863, 1937; Max, Tr. 5996; Garmon, Tr. 3515)

37. A distributor who decides to leave the business may receive a refund on the price of the Sales Kit and Product Kit. (Halliday, Tr. 6615)

38. Most new Amway distributors have had no selling or business experience. (CX 1000–K; Van Andel, Tr. 1695)

39. The vast majority of Amway distributors, including Direct Distributors, conduct the Amway business on a part-time basis, and have another full-time occupation. (Halliday, Tr. 6235; RX 329) [13]

40. Anyone who has become an Amway distributor prior to August 31 of any year or who has continued his distributorship for that year must renew his distributorship authorization for the next year by December 31. (Halliday, Tr. 6484)

41. The number of active distributors since 1972 has remained relatively constant, fluctuating around 300,000, climbing in 1977 to about 360,000. (RX 383)

42. The average annual turnover of Amway distributors is about 50%. The turnover rate for Amway distributors during their first year is almost 75% and thereafter about 25% a year. (CX 909; RX 83)

43. Currently about half of all Amway distributors were sponsored by a Direct Distributor or by a distributor sponsored by a rect Distributor. More than 70% were within three positions of a rect Distributor and 99% were within seven positions. (RX 423)

44. If distributors leave Amway, any distributors whom they may e sponsored move up the line of sponsorship to the next qualified ributor. (RX 331, p. 17–B)

. In order to receive the benefits of sponsoring, Amway ibutors must train their sponsored distributors and stock tory to supply them. (RX 331, pp. 17–B to 18–B)

The distributors sponsored by an Amway distributor become ers of that distributor's "personal group." The sponsored distributors may then sponsor other distributors, thereby forming their own personal groups and enlarging the personal group of the first sponsoring distributor. (CS 1096, p. 2–B) [14]

47. When distributors qualify as Direct Distributors, they "break off" from the personal group of their sponsor, thereafter dealing directly with Amway. (RX 331, p. 8–B)

48. The Amway Sales and Marketing Plan provides communication with distributors through literature published by Amway and by meetings. About 10 or 15 times a year sales rallies consisting of several thousand distributors are held around the country, to which any distributor in the area is invited. An afternoon meeting for high volume distributors only (with no guests allowed) is followed by an evening sales rally for all distributors and their guests. (Van Andel, Tr. 1761–63) These evening sales rallies involve presentation of sales awards with impromptu speeches by the recipients and motivational speeches by other successful distributors and celebrities. "Amway officials are present to offer helpful advice to both new and experienced distributors alike." (*Id.;* CX 62–Z–42 - 43) Area meetings are produced independently by Direct Distributors for their groups or for a combination of Direct Distributor groups. They provide information and inspiration for the distributors. (CX 62–Z–43)

49. About five thousand distributor-operated meetings are held each week. These local meetings help sponsors "build enthusiasm within their group through weekly meetings in their homes or offices for the purpose of training, motivating and sponsoring." (CX 62–Z–43)

Compensation

50. Amway distributors earn income from retail sales through the "basic discount" (the difference between the price paid by the distributor for the product and the price charged by the distributor at retail). A distributor does not make money directly by selling products to his sponsored distributors "because he sells them for the same price he paid for them; the distributor cost." (RX 331, p. 3–B) Instead, distributors receive a [15] "performance bonus" which is paid by Amway through sponsoring distributors and is based on the distributor's total monthly sales volume. The "Basic Discount" and "Performance Bonus" are defined as (RX 331, p. 4–B):

> Basic Discount: When you personally sell Amway products you earn income in two ways . . . the first of these is your "basic discount." You buy products from your sponsor at the wholesale price, and sell them to customers at retail. The basic discount on most home-size products is 35%, with some at 15% or 25%. That percentage is your

immediate income — your "basic discount" — which you get as soon as you are paid by your customers. Most distributors average 30% of Business Volume as income.

Performance Bonus: The second way you earn income is through your monthly Performance Bonus on Amway products you purchase for resale. In addition to your immediate basic discount, you earn a Performance Bonus each month based on total Point Value and BV of all products purchased by you during the month. This is a percentage Bonus which varies from 3% to 25% depending on your total monthly Point Value, according to the schedule below.

PERFORMANCE

BONUS SCHEDULE

Performance Bonuses are paid in addition to the basic discount, which averages 30%.

IF YOUR TOTAL MONTHLY POINT VALUE* IS:	YOUR PERFORMANCE BONUS IS:
7,500 or more points	25% of your Business Volume
6,000 to 7,499 points	23% of your Business Volume
4,000 to 5,999 points	21% of your Business Volume
2,500 to 3,999 points	18% of your Business Volume
1,500 to 2,499 points	15% of your Business Volume
1,000 to 1,499 points	12% of your Business Volume [16]
600 to 999 points	9% of your Business Volume
300 to 599 points	6% of your Business Volume
100 to 299 points	3% of your Business Volume
Less than 100 points	0% of your Business Volume

* Total monthly PV includes both personal PV and PV of others you sponsor.

51. The performance bonus schedule was previously based on monthly dollar purchase volume. (CX 61, p. 4-B) In 1975, in order to adjust for inflation, each product was assigned a "point value" which remains constant regardless of changes in the price of the product. (CX 680-A)

52. Each Amway product is also assigned a dollar value for the purpose of calculating "business volume" ("BV"), corresponding approximately to the suggested resale price of the product, less a warehouse charge. (RX 331, p. 4-B)

53. The performance bonus system provides an incentive to sponsoring distributors to provide training, motivation and supply to sponsored distributors, since they receive income based on the accumulated total sales of all of the distributors in their personal group. (Van Andel, Tr. 1863-64) This payment has been termed "overwrite," "bonus," and "refund," and since 1975 "performance

bonus." (CPF 199) It corresponds to the compensation paid by manufacturers to wholesalers. (Cady, Tr. 5776–78)

54. Under the Amway Sales and Marketing Plan it is the Direct Distributors' duty to see that performance bonuses, which they receive monthly from Amway, are promptly distributed to sponsored distributors and redistributed in that month to all distributors in the Direct Distributor's personal organizations who earned the performance bonus. (RX 331, p. 19–B) Amway enforces its refund policy. (CPF 204) The ADA arbitrates disputes concerning the refund policy. (CPF 205) [17]

Sponsoring

55. The sponsoring distributors earn income on the basis of the total sales volume of their personal distributor group, as well as their own personal retail sales. (RX 331, p. 5–B) Sponsoring distributors must supply and train distributors they sponsor. (RX 331, p. 17–B)

56. Distributors are urged to sponsor new distributors in order to "earn on what others sell" (RX 331, p. 5–B), but the Amway Sales and Marketing Plan stresses that combined retail selling and sponsoring are equally essential to the distributor's success. (RX 331, p. 1–B)

57. About 25% of Amway distributors sponsor new distributors. (RX 415; Van Andel, Tr. 1828; Max, Tr. 6023)

58. Recruiting distributors occurs primarily at an "Opportunity Meeting" which each distributor is urged to hold at least once a week. (CX 68–D) Amway encourages that recruiting be done individually rather than at mass meetings. (CX 638–H) Recruiting new distributors through the presentation of the Amway Sales and Marketing Plan involves (1) introducing the company and products, (2) appealing to the financial goals of the prospective distributors, and (3) explaining the compensation of a distributor through retail and wholesale sales. (RX 331, Section D)

59. The Amway Career Manual for distributors explains how to recruit distributors by appealing to the financial goals of prospects. (RX 331, pp. 1–D to 3–D). The suggested presentation provides that the distributor should: [18]

> Announce to your guests that you would like to tell them about an exciting opportunity to be in business for themselves and to develop an income of as much as $1,000 per month. Explain that it is an opportunity that grows as they share it with others.
>
> Ask if they are as successful as they would like to be. If not, would they be interested in a chance to realize their dreams through a business of their own that

they can build on a part time basis — and, with such a modest initial expenditure? An opportunity does exist that will give them such a chance.

* * * * * * *

[The distributor is then advised to give a short history of the company and to describe some of the products and sales literature.]

* * * * * * *

What does all this mean to you? It means you can become a part of a dynamic growing organization. It means that this opportunity can mean the realization of your dreams.

(Ask questions to find out what the goals and dreams of each prospective distributor may be.)

What are some of your dreams?

Do you want a new car, a new house, college education for your children?

Do you want retirement income that will afford you a comfortable standard of living?

What income do you want six years from now?

Are you willing to work hard to get this?

How much extra money per month do you need for that new car? [19]

$100 a month or more?

What kind would you like — a Chevrolet, Pontiac, Oldsmobile?

How much money per month do you need for that new house?

What kind of home do you want — a three-bedroom ranch — with a price tag of $35,000 - $40,000?

How much will you need for monthly payments — $250, $300 a month?

How much will it take to send the youngsters through college — $2,500 to $3,000 a year for each youngster?

If you could earn an extra $250 a month, you would have an additional $3,000 a year. This might be sufficient to send one youngster through one year of college.

How much would you like as a continuing income — $1,000 a month?

Would you work for your goal?

Would you be interested if I could show you a way you can make your dreams come true?

Would you be interested in a way to achieve this on a part-time basis?

What would you be willing to give up to get this?

You can realize the achievement of your dreams through the Amway Sales and Marketing Plan. It is broad enough for you to achieve whatever your goal is. First of all, you start like everyone else — you are sponsored by another Amway distributor. You are in business *for* yourself, but not *by* yourself. You buy Amway products at wholesale from your sponsor, and you sell them at retail to your customers. (Emphasis in original.) [20]

60. The Amway Career Manual for distributors explains the nature of retail and wholesale compensation provided in the Amway Sales and Marketing Plan. (RX 331, pp. 5-B through 7-B): [21]

HOW MUCH CAN YOU EARN?

PUT IT THIS WAY . . .

for a small business of your own . . . **EXAMPLE 1:** by making only two average sales of $5.00 each per day, working less than an hour in each of 20 days per month, you can sell $200.00 BV per month.

Your 30% average immediate income on $200.00 sales (at BV)	= $60.00
Plus . . . 3% Performance Bonus on $200.00 in BV provided your monthly Point Value is 100 points or more	= 6.00
EQUALS . . . YOUR TOTAL MONTHLY INCOME . . .	$66.00

GROUP SPONSORSHIP

HOW YOU EARN ON WHAT OTHERS SELL

You have seen how you earn an immediate basic discount on each Amway product you sell and how you receive a monthly Performance Bonus based on the total Point Value and BV of all Amway products you sell. Here is still another Amway Career Opportunity: becoming a sponsor:

Every Amway distributor may sponsor other distributors. When you sponsor a new distributor, you become his wholesale supplier, just as your sponsor wholesales to you. Your income from sponsorship comes in the form of a greater monthly Performance Bonus percentage. Your total Point Value and BV include your personal Point Value and BV plus that of those whom you sponsor . . . when all the sales are added together you will probably be in a higher Performance Bonus percentage bracket, and thus earn a larger Performance Bonus. Out of this, you pay the distributor you sponsor his own earned Performance Bonus, but because your total Point Value and BV are greater than that of any of the distributors you sponsor, you will usually earn a larger Performance Bonus than you pay out. You not only earn income on the BV of the distributors in your personal group, but will usually also earn a higher Performance Bonus percentage on your own personal BV.

And you earn in the same way on the new distributors that you sponsor . . . and on those they sponsor . . . and so on. You form a growing group of distributors, and every dollar of BV generated by those in your personal group is a dollar of additional BV for you.

When you're a sponsor, you're building income for your family today, potential income for your retirement, and income that may become part of your estate. That's why Amway is not "employment," but rather, a real career: a growing, repeat business of your own!

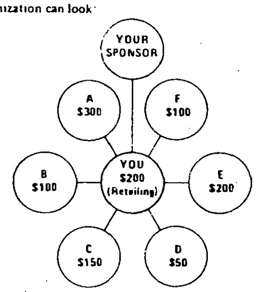
EXAMPLE 2:

Let's assume that you sponsor two other distributors and that each of the three of you sell exactly $200 (at BV) in a month, or $600 (at BV). If the Point Value of these products is at least 600 points, you will receive a $54 Performance Bonus. Out of this, you pay Performance Bonuses of $6.00 to each of your personally sponsored distributors, a total of $12, leaving you $42. This plus your $60 in basic discount gives you a total income of $102 in that month.

In order to retain the right to earn Performance Bonuses on your group BV, you yourself must make not less than one sale at retail to each of 10 different customers each month and produce proof of such sales to your sponsor and Direct Distributor. This provision assists you in maintaining the balance between sponsoring and retail selling which is essential to a successful distributorship.

EXAMPLE 3:

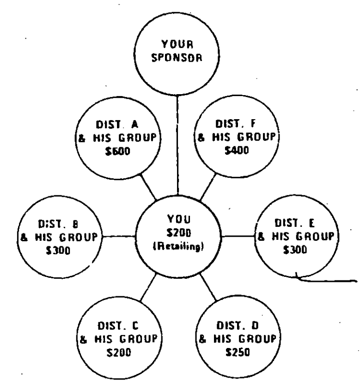
Let's say you have sponsored six distributors. The amount of BV which each will generate will probably vary depending on the length of time they have been distributors and the amount of time they have available for developing their business. The following is an example of how your organization can look:



Immediate income on personal sales $200 (at BV)			**$ 60.00**
Your total group BV:	**$1,100.00**		
Performance Bonuses you receive (12%, assuming a Point Value of at least 1,000 points)		**$132.00**	
Performance Bonuses you pay out (assuming necessary Point Values have been achieved by each distributor)			
Distributor A (6%)	**$18.00**		
B (3%)	**3.00**		
C (3%)	**4.50**		
D (0%)	**.00**		
E (3%)	**6.00**		
F (3%)	**3.00**	**–$ 34.50**	
Performance Bonus you keep:			**$ 97.50**
Total monthly gross income.			**$157.50**

EXAMPLE 4:

As your business continues to grow and as you train and motivate your personally sponsored distributors to retail and to duplicate themselves by sponsoring new distributors, here is how your total BV and income can increase

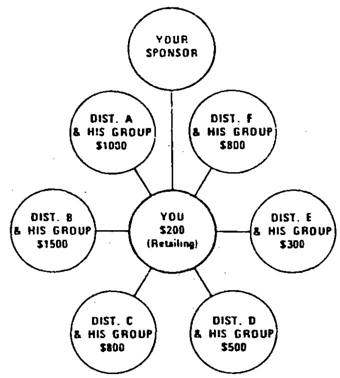


Immediate income on personal sales $200 (at BV)			$ 60.00
Your total group BV: $2,250.00			
Performance Bonuses you receive (15%, assuming Point Value of at least 1500 points)		$337.50	
Performance Bonuses you pay out (assuming necessary Point Values have been achieved by each distributor)			
Distributor A (9%)	$54.00		
B (6%)	18.00		
C (3%)	6.00		
D (3%)	7.50		
E (6%)	18.00		
F (6%)	24.00		
Total paid out		−$127.50	
(Distributors A, B, C, D, E, and F will, of course, be responsible for paying Performance Bonuses to their distributors.)			
Performance Bonus you keep:			$210.00
Total monthly gross income:			$270.00

EXAMPLE 5:

At this point, your business has started to bring you good returns. Although you should have sponsored additional distributors in the meantime, for the purposes of simplification, we will show only six distributors personally sponsored by you. Your part-time business can expand rapidly from this point onward.

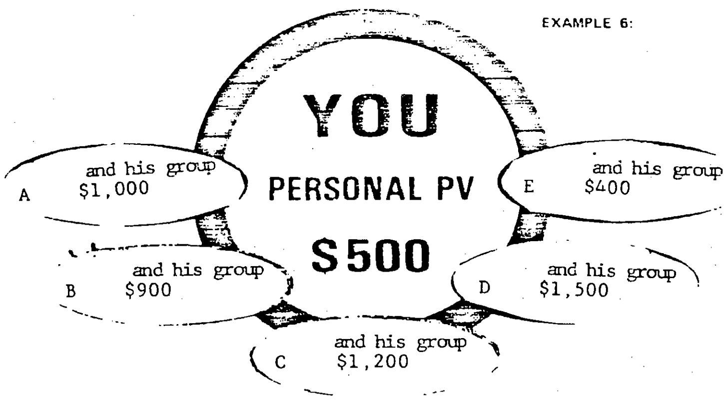
As your distributors' BV grows, so does yours. Your income picture for the month can now look like this



Immediate income on personal sales $200 (at BV)			$ 60.00
Your total group BV: $5,100.00			
Performance Bonuses you receive (21%, assuming Point Value of at least 4000 points)		$1,071.00	
Performance Bonuses you pay out (assuming necessary Point Values have been achieved by each distributor)			
Distributor A (12%)	$120.00		
B (15%)	225.00		
C (9%)	72.00		
D (6%)	30.00		
E (6%)	18.00		
F (9%)	72.00		
Total paid out		−$ 537.00	
(Distributors A, B, C, D, E, and F will, of course, be responsible for paying Performance Bonuses to their distributors.)			
Performance Bonus you keep.			$534.00
Total monthly gross income:			$594.00

FULL TIME SPONSORSHIP INCOME

EXAMPLE 6:



BUILDING TOWARD A DIRECT DISTRIBUTORSHIP

If you work consistently toward building a Sales Group of distributors and increasing your own volume of retail sales, your monthly volume can look like this. See Chart below for income breakdown. Assume that you are selling to a larger personal customer clientele who makes purchases from you totaling $500 BV of Amway products monthly. Assume the distributors you sponsor have increased their retail sales and have sponsored distributors of their own so that together they contribute an additional $5,000 to your total BV. Now you are in the 21% Performance Bonus bracket, provided you have monthly total Point Value of at least 4,000 points . . . you get your basic discount on your personal BV PLUS 21% Performance Bonus on your personal BV. In addition, you will earn between 21% and the percentage Performance Bonus earned by each of your distributors on his BV. You now earn $711.

Distribution of Performance Bonus on $5,500 Total Group BV – 21%
Performance Bonus $1,155.00 (provided you have monthly total Point Value of at least 4,000 points.)

INDIVIDUAL BV	INDIVIDUAL PERFORMANCE BONUS %*	INDIVIDUAL PERFORMANCE BONUS	% PERFORMANCE BONUS LEFT FOR SPONSOR	$ PERFORMANCE BONUS LEFT FOR SPONSOR
A $1,000	12%	$120	9%	$ 90
B $ 900	9%	$ 81	12%	$108
C $1,200	12%	$144	9%	$108
D $1,500	15%	$225	6%	$ 90
E $ 400	6%	$ 24	15%	$ 60
YOU $ 500			21%	$105
TOTAL PERFORMANCE BONUS: $1,155. PAID OUT: $594			YOU KEEP	$561
			YOUR AVERAGE BASIC DISCOUNT	$150
			YOUR AVERAGE TOTAL EARNINGS	$771

Note A, B, C D & E also have distributors under them helping to make total – From here it is only a short step to Direct Distributor

*Assuming necessary Point Values have been achieved by each distributor

7-B

61. Amway distributorships are not for sale and sponsoring distributors receive no profit from the act of sponsoring. It is only after the sponsored distributor begins to buy products that the sponsoring distributor will receive income. (S. Bryant, Tr. 4063)

Direct Distributors

62. A distributor may qualify as a Direct Distributor with at least 8,500 BV in a single month (assuming a point value of at least 7500 points), and with a personal group point value of at least 7500 points or more for the following two consecutive months, with a gross profit of at least $800 for each of the three consecutive months. (RX 331, p. 8–D)

63. A Direct Distributor becomes eligible for voting membership in the Amway Distributors Association and qualifies for the 3% Direct Distributor Bonus, and Sales Training Bonus, and the Profit Sharing Bonus. (RX 331, pp. 8 and 9–B)

64. Direct Distributors receive 3% of the personal group Business Volume of the Direct Distributors whom they sponsor. At that level both the sponsoring and the sponsored distributors are in the same performance bonus bracket—25%. Therefore, in order to provide the sponsoring distributor with an incentive to continue to motivate and train such a sponsored distributor, the extra 3% Direct Distributor Bonus is provided. To receive the 3% bonus, distributors must be qualified Direct Distributors, by having a qualifying personal group Business Volume excluding the Business Volume of Direct Distributors whom they have sponsored. (RX 331, pp. 8–B to 9–B) If the sponsor of the Direct Distributor does not qualify, then the 3% bonus goes to the next upline sponsor who meets the requirements. (S. Bryant, Tr. 4067–68) [25]

65. Amway pays a sales training bonus to Direct Distributors who sponsor three Direct Distributors for any six months in a year. (RX 331, p. 9–B)

66. Amway has each year paid a "profit sharing distribution" in the form of debenture bonds to all voting members of the Amway Distributors Association. (RX 331, p. 9–B; Halliday, Tr. 6212–13)

67. Amway supplies, trains and compensates Director Distributors. (Van Andel, Tr. 1710, 1850)

68. Direct Distributors supply, train and compensate distributors. They maintain a stock of merchandise and literature, have regular office hours, train distributors through sales meetings and advice, and enforce the Amway Rules of Conduct, including the requirement that monthly performance bonuses be distributed to all distributors in their organization. (RX 331, p. 19–B)

69. Direct Distributors are required to requalify annually on the basis of their sales volume. (RX 331, p. 19–B)

70. The number of Amway Direct Distributors in the United States has grown from about 3000 in 1972 to about 4000 in 1977. (Van Andel, Tr. 1695–96; CX 896) About half of the Direct Distributors started with Amway in the last five years. (RX 434)

71. Distributors who fail to requalify as Direct Distributors generally continue as distributors. Between 1960 and 1976, 3070 Direct Distributors failed to requalify as Direct Distributors, and at the end of that period 75% were still Amway distributors. (RX 434) **[26]**

Pyramid Rules

72. Amway, the Direct Distributor or the sponsoring distributor will buy back any unused marketable products from a distributor whose inventory is not moving or who wishes to leave the business. (RX 331, p. 17–B to 18–B; CX 847; CX 1076) The buy-back rule has been in existence since Amway started. (CX 1041–J) Amway enforces the buy-back rule. (CX 847; Brown, Tr. 5012–13; Bortnem, Tr. 686, 690; Soukup, Tr. 913)

73. To ensure that distributors do not attempt to secure the performance bonus solely on the basis of purchases, Amway requires that, to receive a performance bonus, distributors must resell at least 70% of the products they have purchased each month. (RX 331, pp. 16–B to 17–B) The 70% rule has been in existence since the beginning of Amway. (S. Bryant, Tr. 4086) Amway enforces the 70% rule. (Lemier, Tr. 192–93; S. Bryant, Tr. 4056–59; Halliday, Tr. 6497)

74. Amway's "ten-customer" rule provides that distributors may not receive a performance bonus unless they prove a sale to each of ten different retail customers during each month. (RX 331, pp. 1–B and 17–B) The Direct Distributors have the primary responsibility for enforcing the ten-customer rule in their own group. (S. Bryant, Tr. 4061–62) The ten-customer rule was started by Amway about 1970. Prior to that, there was a 25 sales rule which required the distributor to make 25 retail sales a month without regard to the number of customers. (S. Bryant, Tr. 4085–86) The ten-customer rule is enforced by Amway and the Direct Distributors. (CX 823; Case, Tr. 3414–15; Medina, Tr. 4197; Zizic, Tr. 4138–43; Lincecum, Tr. 1266)

75. The buy-back rule, the 70% rule, and the ten-customer rule encourage retail sales to consumers. (Van Andel, Tr. 1999–2000, 2010; Halliday, Tr. 6231–33; Lemier, Tr. 176; Cady, Tr. 5795–97) **[27]**

Operation of the ADA

76. The voting members of the ADA meet once a year for a one day meeting. They elect the Board members of the ADA and receive reports concerning the Amway business. (Halliday, Tr. 6174–75)

77. The ADA Board meets four times a year, usually for two days at a time. (Bass, Tr. 42)

78. Amway uses the ADA Board to receive recommendations concerning the business. Amway presents proposals for changes of rules to the Board for information and advice, and for reaction from the field. (Halliday, Tr. 6612–13)

79. Amway consults with the Amway Distributors Association, through the Board of Directors, in setting up discount and refund schedules, bonuses, and retail prices. (CX 22–B) In its 1975 annual report to the state of its incorporation, the ADA reported that its purpose was (CX 3–A): "To act as a trade ass'n for the purpose of setting policies with the company from whom purchases are made and the pricing of all products sold direct to the consumers." (*Also see* CX 4–A - B for 1971 report.) The Board of the ADA has in fact consulted with Amway about retail prices, *e.g.,* discussing in 1973 price cutting on a cookware promotion. (CX 376–B)

80. The ADA Board also acts as a board of arbitration in disputes among distributors and as an appeal board when Amway has terminated or disciplined a distributor. The ADA Board conducts formal hearings through a hearing committee of three members. Participants may attend the hearing in person and may be represented by an attorney. The hearing committee receives witness testimony and other evidence, and a transcript of the hearing is made if a participant requests it. The committee then makes a recommendation to the Board. The Board considers about 5 or 6 cases each time it meets and in about 20% of the cases the Board disagrees with Amway. Amway always has acceded to the Board's decision. (RPF 243, 244) [28]

Vertical Restrictions

Cross-Group Selling Rule

81. Amway distributors agree to sell at wholesale only to distributors they have sponsored, and to buy only from their sponsor. This restriction is known as the "cross-group selling rule": "*Rule 3. No distributor shall engage in cross-group selling.* A distributor in one line of sponsorship must buy all of his Amway products and literature supplies from or through his supplier." (RX 331, p. 15–B)

82. The cross-group selling rule provides Amway distributors with an incentive to recruit distributors and to train and motivate

them to sell Amway products, since the sponsoring distributor receives income on the sponsored distributors' sales volume. (Patty, Tr. 3111–13; Halliday, Tr. 6237–39; Van Andel, Tr. 1751) Effective sponsoring distributors keep inventory of Amway products, hold sales meetings, run contests and conduct other promotional and training activities. (RPF 159)

83. Amway distributors may transfer from one sponsor to another after being terminated or remaining inactive for six months. Amway also approves about 100 transfers of distributorships a year for other reasons. (RX 331, pp. 18–B and 19–B; Halliday, Tr. 6507-09)

84. A distributor must train and supply his sponsored distributor. If they are in different geographic locations, however, the sponsor may arrange, through his Direct Distributor, to have the sponsored distributor trained and supplied by a Direct Distributor living in the sponsored distributor's area. (RX 331, p. 17–B) In these private servicing arrangements, the two Direct Distributors determine the compensation for this service. (Van Andel, Tr. 1739–41) [29]

Retail Store Rule

85. Amway distributors agree not to sell in retail stores (RX 331, p. 16–B):

RULE 6. No distributor shall permit Amway products to be sold or displayed in retail stores, PX's, ships or military stores; nor shall he permit any product displays to appear in such locations, even if the products themselves are not for sale. No Amway literature shall be displayed in retail establishments.

A distributor who works in or owns a retail store must operate his or her Amway business separate and apart from the retail store. Such distributors must secure customers and deliver products to them in the same manner as Amway distributors who have no connection with a store. Other types of retail establishments, which are not technically stores, such as barber shops, beauty shops, etc., likewise may not be used to display Amway products.

86. Amway prohibits distributors from setting up displays or booths at fairs, home shows, or other similar special events. (RX 331, p. 23–B)

87. Amway restricts its distributors in their sales of Amway products in fund-raising drives carried on by churches, and other civic or charitable organizations, limiting the manner and time of the sales and the products to be sold. (RX 331, p. 15–B; CX 277–M – N)

88. The retail store rule gives an incentive to Amway distributors to provide services to consumers. Amway distributors go to the consumer's home, demonstrate and explain the products, help with cleaning problems "on site," and deliver the products to the consumer's home at the customer's convenience. These services are

typically unavailable from a retail store. (Schroeder, Tr. 5355–56; Bryant, Tr. 4396; Halliday, Tr. 6240–43; Max, Tr. 5893–94) [**30**]

89. In the absence of massive advertising to create demand, sales of Amway products in retail stores would fail. Retail stores might be willing to stock Amway products in the short run because of existing demand created by personal direct selling by Amway distributors. (Cady, Tr. 5785–86) Distributors would quit or switch their attention from consumers to stores. (Cady, Tr. 5786) Demand would therefore slow and when demand slows down there is no longer shelf space available in the store. (Van Andel, Tr. 1810–12) If Amway were to sell through retail stores, "they would destroy their direct selling capability." (Diassi, Tr. 5537–38)

Customer-Protection Rule

90. The Amway Sales and Marketing Plan formerly had a "customer protection rule," providing that, upon making a sale to a retail customer, a distributor established an exclusive right to resell to that customer for a specified period of time. (CX 60–Z–5)

RULE 1. *A distributor who completes a sale to a retail customer and registers such sale thereby establishes the exclusive right for a period of the next 30 days to re-sell that customer.*

An Amway distributor, upon completing a sale to a retail customer, thereby establishes the exclusive right to re-sell Amway products to that customer, provided he has "registered" such sale by sending a copy of the sales receipt to his Direct Distributor or *to such sponsor as the Direct Distributor may designate.* The distributor must sell the retail customer an Amway product and register that customer each 30 days in order to retain his exclusive right on a continuous basis.

In the case of a commercial account, a distributor may retain an exclusive right to his customer in the same manner except that the exclusive right shall be effective for a period of 90 days. [31]

If the 30 or 90-day exclusive period is permitted to expire because of a failure to make and register a sale, then the next distributor to complete a sale and register the customer thereby establishes a new exclusive right period during which such exclusive right shall remain in effect in accordance with the terms outlined above.

Whenever a distributor approaches a new prospective customer, he shall ask whether that prospective customer is presently being sold regularly by an Amway distributor. If the customer is being sold regularly, then the distributor shall make no further attempt to sell that customer, but shall refer the customer to his or her regular distributor. (Emphasis in original.)

This rule was carried over to Amway from the Nutrilite sales plan. (Van Andel, Tr. 2047–48)

91. The Amway Sales and Marketing Plan formerly provided

that a distributor had an exclusive right to sponsor his own customer as a distributor. (CX 60-Z-5)

92. In January 1972, effective March 1, 1972, Amway abolished the "customer protection" rule and the rule giving a distributor the exclusive right to sponsor his customer as a distributor. (CX 284; CX 293)

93. Amway continues to support the principle of the customer protection rule. In June of 1974, Mr. Halliday, one of the three top officials at Amway, spoke at a New Direct Distributors' meeting. He pointed out that, while legal, it was unethical to "go in cutting out another Amway distributor" by taking his commercial account: "[S]ometimes there's a—something above and beyond the law that you have to think about in terms of ethics." (CX 1041-I) [32]

Advertising Regulation

94. Only Amway Direct Distributors are permitted to display the Amway name on the exterior of their distributor office, and that office must be for wholesale only. (RX 331, p. 20-B)

95. Amway controls the display of the Amway name and logo on distributors' business vehicles by approving their use only if the distributor meets specific instructions involving the display of the Amway trademark, trade name, logo, design or symbol, and the condition of the vehicle. (RX 331, p. 21-B)

96. Amway restricts the use by distributors of the Amway name in telephone directories. For example, only Direct Distributors may appear under the Amway or Nutrilite names in the white pages. Other Amway distributors are allowed to use the designation "Amway Distributor" in the white pages, as long as they are listed under their surname. (RX 331, pp. 21-B - 22-B) In the yellow pages, upon prior written approval by Amway, a distributor may list under three specified categories, ("cleaning products," "cosmetics," and/or "vitamins") using the designation "Amway Home Products Distributors." (RX 331, p. 22-B)

97. Only upon prior Amway written approval, may distributors use outdoor advertising on billboards or signs. (RX 331, p. 23-B)

98. Amway distributors may not use the Amway trade name or logo on checks except to describe themselves as Amway distributors. (RX 331, p. 23-B) [33]

99. Direct Distributors may contract for local advertising of Amway products on radio, television, or in newspapers only by using advertising mats and scripts obtained from Amway. (RX 331, p. 23-B)

100. If Amway distributors use the Amway name in classified

recruiting advertisements, the advertisements must follow the exact, word-for-word copy of one of seventeen formats provided by Amway. For example: "Local Amway Distributor is helping many persons earn money working two to four hours a day. We can help you. For interview, call ——————————." (RX 331, p. 24-B)

101. All Amway printed material is copyrighted and may not be reproduced by distributors without permission. (RX 331, p. 24-B)

102. Amway restricts the advertising of its distributors in order to keep a consistent market position, among other reasons. (Cady, Tr. 5815)

103. People inexperienced in direct sales tend to overestimate the effectiveness of advertising which may increase their expenses and hasten their exit from the market. (Cady, Tr. 5813-15) The Amway direct sales system is based on the plan that personal contact is more effective than advertising in selling Amway products and recruiting distributors. (Van Andel, Tr. 1857-58)

104. By its regulation of distributors' advertising, Amway attempts to assure that its marketing plan is explained and represented by experienced distributors. (Halliday, Tr. 6244-46; CX 960) [34]

105. With the high turnover rate typical of direct sales organizations, Amway attempts to control the distributors' advertising in order to avoid the negative impact on consumers responding to ads placed by distributors who have gone out of business. (Halliday, Tr. 6244-46; Cady, Tr. 5812-16)

106. Amway uses and has registered 125 trademarks and servicemarks. (RX 336)

107. Amway has controlled the use of its trademarks, servicemarks, and trade names in order to prevent misrepresentations by some distributors. One distributor in Alton, Illinois, ran recruiting ads implying that he was offering employment. A similar incident occurred in New York City. Amway terminated both distributors. (Halliday, Tr. 6246-49) Some Amway distributors in Kansas City falsely represented that Amway cookware was the same as cookware costing twice as much. Amway took disciplinary action against the distributors. (Halliday, Tr. 6253-54) A distributor in Arkansas produced cassette tapes and literature which misrepresented the Amway Sales and Marketing Plan and Amway products. Amway brought suit and injunctive relief was obtained prohibiting the production and distribution of the materials. (Halliday, Tr. 6254-56) Several distributors in Minnesota produced their own literature advertising several Amway cleaning products including a germicide The literature did not give the proper instructions. Relying on the brochure, a distributor recommended to the owner of a goat farn

that the product could be used to sanitize a goat before milking. The literature failed to give proper instructions, and the goatman applied the germicide at full strength and burned several goats severely. Amway located and destroyed all copies of the unauthorized literature. (Halliday, Tr. 6250-51) [35]

108. Amway also controls the use of its trademarks, servicemarks and trade names to avoid possible liability for the contents of advertising by the distributors. (Van Andel, Tr. 2055) Improper use of its logo on vehicles operated by distributors might imply an employment relationship attaching liability in the event those vehicles are involved in an accident. (Halliday, Tr. 6252-53)

Price Fixing

109. Amway has fixed the prices at which its products are to be sold to distributors and to consumers. One of the "Rules of Conduct" of the Amway Sales Plan published in 1963 was that (CX 53-Z-31):

> No distributor shall sell products sold under the Amway label for less than the specified retail price, when making sales to persons who are not distributors, except where commercial discounts are authorized to be given. No distributor shall give a greater discount than that authorized in the appropriate Amway Product Sales Manual.

Those who signed the application to become Amway distributors at that time agreed to comply with those distributor requirements and "to observe the spirit as well as the letter of the Code of Ethics and Rules of Conduct of Amway Distributors." (CX 53-Z-62) Amway had 30,000 distributors in 1963. (CX 53-H)

110. Amway fixed the charge for freight to be collected by the distributors. In 1963, Amway sold its products to distributors FOB regional warehouse. Amway provided that, since the Direct Distributor picked up the products from the warehouse and incurred freight costs in delivering the products to the ordering distributor: "[The Direct Distributor] may assess a freight charge of 1% of [purchase volume] of each invoice to [36] help offset some of this cost. Each sponsor is authorized to pass this charge down the line . . . ." (CX 53-Z-37 - 38) In a few areas that were long distances from the nearest warehouse, Amway's policy was that "it is permissible to add certain additional freight costs to the retail prices, and to increase retail prices." (CX 53-Z-40)

111. Amway still indicates the price that distributors are to charge at wholesale. The 1963 Amway Sales Plan explained wholesale prices (the prices paid in sales from one distributor to another) (CX 53-Z-15):

When a sponsor buys Amway products from his sponsor or Direct Distributor, and resells them to a distributor whom he sponsors, he both buys and sells at the basic discount. Thus products sold between distributors are always sold at the same price, with no profit made on the immediate transaction. The profit is made later on the refund percentage . . . .

(*See also* CX 88-E - 1968) The 1975 Amway Career Manual for distributors explained wholesale prices (RX 331, p. 3-B):

In Amway, a sponsor does not succeed unless his sponsored distributors succeed. He cannot make money by simply selling products to his sponsored distributors because he sells them for the same price he paid for them: the distributor cost. Instead he makes money on the Performance Bonuses they generate on their Business Volume, which in turn is based on their retail sales. . . . [37]

112. Respondents have fixed the prices at which its products may be sold through fund raising drives.

(a) In the Career Manual for Amway distributors published in 1968, Amway specified the products that distributors could sell through fund-raising drives by schools, churches and clubs, and stated that the distributor should (CX 57-Z-152):

See that standard retail prices are observed. Do not permit cut-rate selling. Cut-rate selling during a fund-raising campaign could hurt your own regular selling of these items.

(*Also see* CX 54-Z-128 - for 1965.)

(b) In the Rules of Conduct published November 1, 1969, Amway stated that the Amway Fund-Raising Plan was that (CX 277-"N"):

The selling organization will buy the products from the distributor at retail and will sell them at retail. Selling organizations will be requested to adhere to the suggested retail prices.

The Amway Plan also specified that (*ibid.*): "The distributor will pay the selling organization a *profit* of not more than *the difference between the retail price and the distributor cost* . . . ." (Emphasis in original.) This part of the rule fixing the amount to be paid to the selling organization by the distributor was recommended by the ADA. (CX 338-B)

(c) The current Amway Rule of Conduct for fund-raising drives specifies the six products which may be sold and states that (RX 3[illegible] p. 15-B):

Members of the selling organization will only take orders for the products. S[illegible] orders will be turned over to the sponsoring distributor, and he, or distributors i[illegible] organization, will deliver the products to the customer and collect the purchase [illegible] [38]

113. The 1965 price list for distributors specified the "retail" price for Amway products. (CX 587) The 1970 price lists specified the the "retail prices (for sales tax purposes)." (CX 593; CX 615) Amway price lists since 1972 have specified "suggested retail for sales tax" (CX 597 - 1972; CX 620 - 1973), or "retail sales comp. base" (CX 598 - 1973; CX 605 - 1976). The current order form states that the price of the Amway products is "suggested retail." (RX 456, RX 460)

114. Amway has a policy of advising distributors not to sell Amway products at discount to commercial accounts. Amway sells training and motivational cassette tapes to distributors for use at sales meetings. Among the "proven ideas from successful distributors" spoken on the tapes is the advice not to grant discounts (CX 1031-I - Transcript of tape sold in 1976, CX 605-M):

> (Don Mumford speaking) So, so anyway, he says, "Don, do you, what kind of a deal do you give? If we order 50 barrels from you, what type of a deal do you give?" They have the same philosophy as Amway. Whether if you buy one case or a thousand cases, it's all the same price. There's no deals. That's what I told him. We don't have any deals. It's all the same price. If it's worth $95 a drum, then 50 drums is still worth $95. I, I'm just telling you this, don't give deals. I don't, it's just not worth it, it's just not worth it. (applause) But anyway, he gave me a blanket order for 50 barrels.

Commercial sales are where price competition among Amway Distributors is most likely to occur. (Halliday, CX 1040-K; CX 485) [39]

115. Amway threatens termination of the distributorship to discourage retail price cutting. In Dallas, Texas, in 1971, Mr. DeVos talked to Direct Distributors and was asked what could be done about price cutting by distributors (CX 1037-E - G):

> Question:] Are you as Amway going to do anything to distributors who are selling products at wholesale to retail customers? [DeVos:] If you have a distributor who is elling Amway products at wholesale to a customer, our action has got to be first of all get a complaint on it and find out who the distributor is that's doing it. Our next ove has got to be to work on his removal, but this isn't an easy problem, because if is person wishes to sell to anybody on the street at whatever price he wants to, ı're getting into some touchy areas on price fixing. Now the only thing you can nt out is that sooner or later the distributor is going to go broke — because you 't go on selling the product at what you paid for it and survive in the business. . . .

DeVos gave the Direct Distributors further advice on how to : to the price cutting distributor. After warning the Direct ributors that price fixing is a serious matter "that the federal ıle and the FTC watch like a hawk" (CX 1037-G):

> do a sales job on the guy and pointing out that if he's going to continue that he's to destroy his own business, he's gonna work at a non-profit situation, he'll tely not be able to recruit distributors, because they can't make any money and

what he's doing is destroying himself, and therefore in most cases where you have it happen it disappears quite rapidly.

[40] 116. Amway combines with distributors who report price cutting and with Direct Distributors so that pressure may be applied to stop distributors who are retailing Amway products at less than the suggested price. In a tape recording of a new Direct Distributor seminar conducted in 1971, by Mr. Halliday, an official of Amway, and one of the three members of the Board of Directors of the company, told the distributors that, in the event that another distributor sells products at a reduced price, they should approach that distributor's Direct Distributor (CX 1040–J):

[Question:] We have had some people who would, uh, sell products at a reduced price, for example, last week we had a fair booth and, um, I knew some of this was going on, once in a while people would come up and I'd just ask them, I'd say, "Say, what, uh, what are you selling shoe spray for in your area?" And, some of the prices that I got were, uh, very staggering to the imagination. What can we do about this?

[Halliday:] Well, again, I think the only thing you can do about it as an individual is to go to talk to the Direct Distributor of that organization, explain to him what he's doing, as far as the image of all Amway distributors, uh, the fact that they're confusing customers — the potential customers, that the reason that the price — you have to get that retail price is if you're rendering the service that you're rendering that's the only way that you're going to be adequately compensated for it. You're gonna have to work with him on an informal basis. As far as our being able to write him and saying "You can't do it." we cannot.

[41] *See also* the testimony of Lawrence Lemier, an Amway Area Coordinator until October of 1973, who had handled complaints from distributors. Occasionally, a distributor would complain that some other distributor was selling products at less than retail price to retail customers. Mr. Lemier would tell both the Direct Distributor of the complaining distributor and the Direct Distributor of the price cutter that (Lemier, Tr. 179):

[T]here was not much Amway could do in a case like that. We couldn't control prices, but I would let them know that studies were made and that products at the retail, the suggested retail price, those were fair prices to the retail customer and a fair margir of profit to the distributor.

117. This record contains examples of the success of Amway' policy of combination and communication to stop price cutting. I 1972, Lorraine Cooke, an Amway distributor from Gun Lak Michigan, distributed flyers featuring Amway products at belc suggested retail prices. Other distributors reported this to Amw and Lorraine Cooke received the following letter dated June 8, 19 from Ann Penrose, an Amway Administrative Legal Assistant (831–A – C):

Amway Corporation will not tolerate the use of the Amway name, logo, or its products in any manner in privately developed promotional literature. We, therefore, must instruct you to immediately cease and desist the dissemination of both flyers and to destroy any remaining quantities which you may have in your possession.

* * * * * * *

One of your flyers also indicates that you are apparently selling Amway products at a price below Amway's suggested retail prices in a "package special." [42]

As you will note from the SA-13 Wholesale Price List, Amway publishes a suggested retail price list for sales tax purposes. Amway, however, cannot impose a fixed price schedule upon its distributors. Under the Amway Sales and Marketing Plan, each Amway distributor is an independent businessman who purchases products from Amway for cash. Title to these products actually passes from the company to the distributor (and later from distributor to distributor or from distributor to retail customer) under a purchase and sales agreement. At each sale, title passes to the buyer immediately upon purchase. Thus, in essence, each buyer has latitude in determining what price he will charge for the product when he subsequently sells the same.

There are certain built in features about the Amway Sales and Marketing Plan which tend to discourage unreasonable and unrealistic price variances. Perhaps the most important of these is that any price reduction results in less net income to the distributor. The product line manufactured by Amway Corporation is relatively stable, with several new products being added each year, and several products being removed from the line. Generally speaking, the product line remains essentially constant, particularly compared with some other direct selling companies, such as Avon, which have a calculated policy of conducting "sales" every several weeks in order to generate consumer interest and which ties into their constantly changing line of products and packaging.

A policy of "sales" is not consistent with a stable product line, since customers would become confused concerning why there would be a "sale" one month and not during the next. They would lose confidence in the stability of the distributor with whom they are dealing, at least from the standpoint of individual pricing policies. [43]

Then, again, the Amway products, because of their concentrated nature, and the ıanner in which they perform, compete effectively with other products designed ıbstantially for the same purpose and which are available in retail stores. Because of ır advantageous competitive position, the practice of "sales" is not, and would not be, a similar benefit, or would not produce the same results in increasing volume, as is pected by a grocer or supermarket when it embarks upon the same practice.

We are usually able to point out to a distributor that it is to his financial advantage naximize his profits by selling Amway products at the suggested retail price for s tax purposes. Because of certain intricacies of federal law, and those of some ᴈs, it is not possible for Amway Corporation to dictate to independent Amway ·ibutors the prices at which they should sell an Amway product. It has never been ssary for Amway to take any position such as that for the reason that the vast rity of Amway distributors, which means almost 100% of all Amway distributors, ware of the principle stated in this letter and are thus more than content to realize the greatest maximum profit on their sales of Amway products. Therefore, we would certainly discourage any such "sale."

Lorraine Cooke wrote back to Ann Penrose, stating that she had "complied with all your demands" (CX 1008):

I have always through the course of my lifetime—and in my experience as a Girl Scout Leader—preached and tried to practice Fair Play. . . .I cannot tell you how dreadful this has been to me. I am a new distributor—this has been a good lesson to me. . . .and needless to say, I have CAREFULLY re-read my manual and now understand them (sic) more fully. [44]

If I have hurt anyone, in my ambitions to get started in the Amway world, please advise how I may further correct my mistakes. They were certainly. . . .not intended to hurt, please believe me.[3]

Steven A. Bryant, Amway's Chief Attorney, wrote to Mrs. Cooke shortly afterward, when another distributor alleged that Mrs. Cooke had told customers that the area in which she sold was her "territory." Mr. Bryant warned that because of the complaints [including the price cutting episode] concerning her, Mrs. Cooke was in danger of losing her distributorship. He sent a carbon copy of his letter to Mrs. Cooke's sponsors, requesting that they "educate this distributor as she was causing considerable disturbance in the field." (CX 1017)

118. Amway warns against writing letters to distributors concerning price cutting, to prevent the Federal Trade Commission from obtaining them. (DeVos, CX 1037-G, I)

119. Amway's policy is that distributors who advertise Amway products at discount in the newspaper can have their distributorships terminated. (DeVos, CX 1037-I)

120. One of Amway's Rules of Conduct requires distributors to buy back from a sponsored distributor who is leaving the business any marketable products, literature or sales aids, with a 5% discount for handling. (RX 331, pp. 17-B to 17-C) If the distributors do not buy back the products or promotional material, Amway will. (CX 406-C) [45] There are two reasons for the buy-back policy: (1) to prevent inventory-loading, and (2) to avoid discount sales by distributors who may choose to leave the business. (CX 406-D)

121. An example of the execution of the buy-back rule to stop price cutting involved Russell Bortnem, an airplane pilot who had been an Amway distributor for five years. He had sponsored 20 to 30 distributors and had between 75 and 100 in his organization. (Tr. 684) Since his sponsor had moved away, he was authorized to buy

[3] See also Holdridge, Tr. 781-82 and CX 833 for a similar episode.

directly from Amway and service his distributors from the inventory he kept. He built up too much inventory and Amway would not buy back certain products which had been discontinued or the size of which had been changed. Russell Bortnem and three other distributors placed an ad in the Fort Lauderdale newspaper on October 26, 1975, advertising Amway products "Below Wholesale! 'Our loss, your gain'." Mr. Bortnem testified (Tr. 689):

Q. You placed the ad approximately in October, '75, October 26, '75?

A. Yes. I think it ran probably three days throughout a week or a week and a half period.

Q. Did you receive any response from that ad, you personally?

A. Yes. We sold quite a few things but also most of the response was from other direct distributors in the Fort Lauderdale area.

Q. What did direct distributors respond?

A. They were threatening us that, "You can't do this and we are going the [sic] report you to Amway," and everything. . . .

[46] In a few days he received a call from an Amway employee who asked him to remove the ad from the paper and who agreed to buy the inventory. (CX 1049, CX 1050) Mr. Bortnem had indicated previously that he would resign his Amway distributorship if that was what was required to be able to return the Amway products (RX 10). The buy-back agreement prepared by Amway provided that in return for the reimbursement, Mr. Bortnem agreed to relinquish his Amway distributorship. (CX 1050)

122. Amway urges distributors to buy back products even if the products are no longer marketable so that they will not be sold at discount. (Halliday, CX 1040-N, CX 1042-D - E)

123. Amway instructs its distributors that when Amway products are in the possession of shipping companies, salvage stores or freight recovery stores, which acquired the products by paying off insurance claims on damaged freight, the distributor should repurchase the products or notify Amway so that Amway can repurchase them. The reason for this policy is to prevent salvage stores from discounting the products. (CPF 227)

124. Amway collects retail sales taxes at the time of sale to Amway Direct Distributors and pays the state governments. This system was started at the request of state taxing authorities. (Van Andel, Tr. 1782-83; Fisher, Tr. 3201-04) Amway refunds the prepaid sales tax to distributors who request refunds because the products were not sold at the suggested retail price. (Van Andel, Tr. 1817; RX

328) Part of these refunds undoubtedly go to distributors who have consumed the products rather than having resold them. (Van Andel, Tr. 1994) [47]

125. On commercial sales, the distributor can buy the products from Amway and resell to the commercial account, or the distributor can request that Amway finance the sale. If the distributor cannot afford to buy the products, he can send the order to Amway, and if Amway decides the commercial account has a satisfactory credit rating the products will be shipped directly to the customer; Amway will bill the customer and when payment is received the distributor will receive compensation less 3% for this billing and service. Until at least 1972, the Amway instructions for commercial sales to be financed by Amway instructed the distributor to: "3. Indicate price quoted and whether to be shipped prepaid or collect. If freight collect, price quoted should be PV. If freight prepaid, price quoted should be suggested retail . . . ." (CX 61-Z-60)[4] Amway does not currently specify that the purchase price should include freight collect or prepaid. (RX 331, pp. 8-E to 9-E)

126. Amway distributors take title, dominion and risk of loss over Amway products, except for commericial sales where the distributors ask Amway to provide credit. (CX 831)

127. The vast majority of Amway distributors do not cut the retail price for Amway products. (CX 831-B - C) The number of reports annually received by Amway of price cutting by distributors is usually less than a dozen. (Halliday, CX 1040-H; DeVos, CX 1037-D) [48]

Misrepresentations and Failure To Disclose

128. Amway instructs its distributors to make "only such claims as are sanctioned in official Amway literature." (RX 331, p. 14-B) Amway disciplines, by termination or censure, distributors who misrepresent the Amway Sales and Marketing Plan. (Halliday, Tr. 6262-65, 6488-97; Van Andel, Tr. 1847)

129. Amway literature emphasizes that retail selling is an essential part of the Amway Sales and Marketing Plan and that a distributor cannot succeed merely by sponsoring new distributors. (RX 331, pp. 5-A, 8-D through 10-D)

130. Amway emphasizes that hard work is necessary to succeed as a distributor. Amway tells the distributor:

You have to work to build your business. You have to do the succeeding yourself. Not

[4] "PV" meant purchase volume. (CX 61-T) (See CX 615-C.) Since 1975 this has been called "BV" or "business volume." (Finding 52) (See CX 605-F) The name was changed to avoid confusion with "point value" added in that year. (Finding 51)

us. Not your sponsor. Not your group. You. All we can do is urge you on, support your efforts, ship the products, send the Performance Bonuses.

(RX 331, p. 5–A; see also pp. 3–A, 8–D, 9–D; DeVos, CX 1045–G - 1970; Van Andel, CX 999–J; CX 85–X)

131. Amway literature currently states that distributors should not "quote dollar incomes on specific individuals even though you may want to use their stories about the homes in which they live, the cars they drive, or the airplanes they fly." (RX 331, p. 9–D) [49]

132. Amway representatives have stated specific dollar incomes which may be possible to achieve as an Amway distributor. For example, Mr. DeVos attended an Amway rally in Mobile, Alabama, on February 8, 1973, and in a sales inspirational speech stated that the distributors have "unlimited income potential" because how much they made depended on how much they sold and that:

. . .[Y]ou can start out by trying to make $50 and when you start climbing and working with the plan you can make $100,000 in the same plan. (CX 1007–N)

And, he said:

You ought to open up your mind right now to thinking in terms of making $100,000 a year because you can do it and you ought to think that way. (applause) Listen—That won't happen tomorrow, and it won't happen the next day. But if [you] were to work at any other job you've got 40 years ahead of you. And there are going to be people in this room and in this country who by the time they are 40 starting even part time building gradually, they're going to arrive at a point where they are going to have that kind of income only because you dared think about it. (CX 1007–O)

This statement, in context, meant that only some hard workers would achieve this level of success. It was directed to the "young people in their twenties" in the audience. The story preceding it was of a distributor who was finally able to buy her children a new pair of shoes for school. And Mr. Devos said "there aren't many hundred thousand dollar deals in real estate either." (CX 1007–H) [50]

133. Some Amway distributors do make substantial gross incomes from their Amway business. In fiscal 1971, there were 291 Amway distributors who had a purchase volume of $100,000 or more. About 11% of the Direct Distributors in the years 1972–74 did that well. A few sell $300,000 or more. About 28% of the Direct Distributors have an annual purchase volume of $50,000 or more. (CX 917–A - B) In 1974, about 39% of the Direct Distributors received performance bonuses of $10,000 or more. (CX 918–A - B) Well balanced distributors, according to Amway, keep about one-half of the performance bonus. (RX 401, p. 10) In 1974, about twenty distributors received 3% Direct Distributor bonuses of more than

$20,000, ten received more than $30,000, three received more than $40,000 and one got $56,178.92. (CPF 524) (See RX 401, p. 10.)

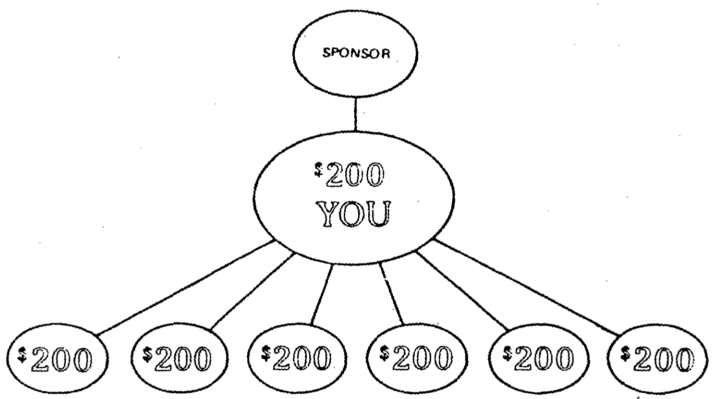
134. Until 1973, Amway explained to new distributors the potential income from retail selling by the representation that (CX 85–T): "By making just one average sale of $5.00 per day, you can sell $100.00 worth of products a month." Later Amway increased the distributors' potential "average gross income" to $200 a month. (RX 331, p. 3–D):

> You can make retail sales that will average $200 BV every month by making "Two sales a day, the Amway Way!" On your $200 in BV, you receive an immediate income of about 30% or $60. (You buy Amway products from your sponsor at varying discounts from 15% to 35%; this averages out at about 30%.) The term "Business Volume" (or BV for short) is used to describe the amount of products that you purchase from your sponsor for your personal customer needs, your own use, and that of the distributors whom you personally sponsor.
>
> You also receive a second income, or a Performance Bonus on your Business Volume (BV), when you have a monthly Point Value of at least 100 points. On $200 BV, your Performance Bonus is 3%, or $6, provided you have Point Value of at least 100 points that month. This means your gross income for the month is $66—a good part-time income for making two sales a day, the Amway way. [51]
>
> ON YOUR $200 IN BV
>
> YOUR AVERAGE GROSS
>
> INCOME IS
>
> $60.00
>
> YOU ALSO RECEIVE A
>
> PERFORMANCE BONUS OF 3% OF $200 BV
>
> OR
>
> $6.00
>
> TOTAL GROSS INCOME
>
> FROM YOUR OWN RETAIL
>
> BUSINESS IS
>
> $66.00

135. Amway instructs its distributors to explain the potential income to be made by sponsoring by "drawing circles." These diagrams are based on Amway's representations that a distributor's potential "average gross income" is a particular amount. Until 1973, Amway used $100 for the amount. (CX 61–Z–31 to Z–35) By 1975,

Amway had increased that amount to $200 BV (RX 331, p. 5–D through 7–D): [52]

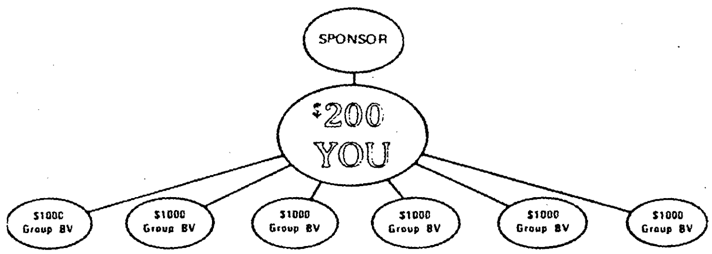
FOR DISCUSSION PURPOSES, LET'S ROUND OUT THE NUMBERS TO $200.00. I'M SURE YOU REALIZE THAT SOME WILL DO MUCH LESS AND SOME MORE. BUT, IF THEY MAKE TWO SALES A DAY, THEY SHOULD SELL AT LEAST $200 (AT BV) PER MONTH.



Immediate income on Personal Sales of $200 (at BV)		$ 60.00
Your total Group BV:		
$200 in BV x 7	$1400	
12% Performance Bonus on $1400 (assuming Point Value of at least 1,000 points)	$ 168	
Less Six 3% Performance Bonuses on $200 to your distributors (assuming necessary Point Values have been achieved by each distributor)	– $ 36 Performance Bonus you pay	
	$ 132 Performance Bonus you keep	$132.00
Total gross income from your business		$192.00

YOUR BUSINESS CAN BUILD EVEN LARGER AS YOU TRAIN AND INSPIRE YOUR PERSONALLY SPONSORED DISTRIBUTORS TO DUPLICATE THEMSELVES BY SPONSORING NEW DISTRIBUTORS. LET'S SAY THAT SIX OF YOUR PERSONALLY SPONSORED DISTRIBUTORS SPONSOR FOUR DISTRIBUTORS EACH AND THAT EVERYONE MAKES TWO SALES A DAY, WITH EACH ONE SELLING $200 (AT BV) A MONTH.

YOUR INCOME PICTURE FOR THE MONTH WOULD LOOK LIKE THIS: (HERE AGAIN FOR THE SAKE OF SIMPLICITY, WE HAVE ROUNDED OUT THE NUMBERS TO $200.)

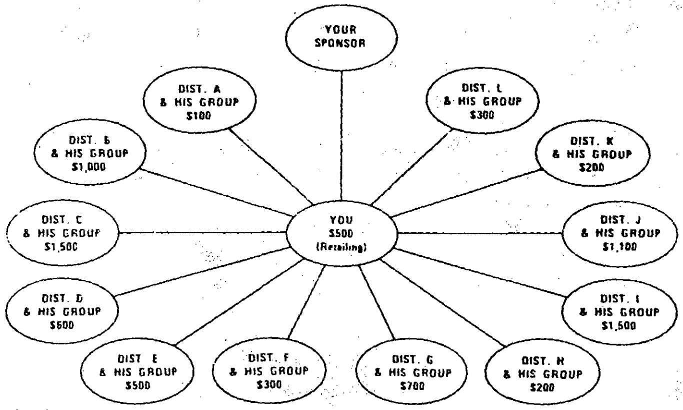


Immediate income on personal sales of $200 BV		$ 60.00
Your total Group BV:		
$200 in BV x 31 or 6 groups of 5 distributors plus your own sales	$6,200	
23% Performance Bonus on $6,200 (assuming Point Value of at least 6,000 points)	$1,426	
Less six 12% Performance Bonuses on $1000 to your distributors (assuming necessary Point Values have been achieved by each distributor) who in turn pay Performance Bonuses to their distributors	− $ 720 Performance Bonus you pay	
	$ 706 Performance Bonus you keep	$706.00
Total gross income from your business		$766.00

THE GROWTH OF YOUR PART-TIME BUSINESS FROM THIS POINT ONWARD CAN ONLY BE DESCRIBED BY THE PHRASE – IT EXPANDS RAPIDLY. THE OPPORTUNITY IS THERE FOR YOU TO CONTINUE TO BUILD YOUR SALES ORGANIZATION IN THE SAME WAY UNTIL YOU ATTAIN A MONTHLY POINT VALUE OF 7,500 OR MORE POINTS. IT WILL, OF COURSE, REQUIRE MORE TIME AND MORE EFFORT, BUT IT CAN BE DONE AS A PART-TIME BUSINESS.

THE DISTRIBUTORS SPONSORED BY YOUR PERSONALLY SPONSORED DISTRIBUTORS SPONSOR OTHER DISTRIBUTORS, AND THUS YOUR GROWTH EXPANDS EVEN MORE.

A DIRECT DISTRIBUTORSHIP CAN HAVE A PROFILE LIKE THIS:



Immediate income on personal sales $500 (at BV)				$ 150.00
Your total group BV		$8,500		
Performance Bonus you receive (25%, assuming Point Value of at least 7,500 points)			$2,125.00	
Performance Bonuses you pay out (assuming necessary Point Values have been achieved by each distributor)				
Distributor A (3%)	$ 3.00			
B (12%)	120.00			
C (15%)	225.00			
D (9%)	54.00			
E (6%)	30.00			
F (6%)	18.00			
G (9%)	63.00			
H (3%)	6.00			
I (15%)	225.00			
J (12%)	132.00			
K (3%)	6.00			
L (6%)	18.00			
TOTAL PAID OUT			– $ 900.00	
(Distributors A, B, C, D, E, F, G, H, I, J, K, and L will, of course, be responsible for paying Performance Bonuses to their distributors.)			$1,225.00	
Performance Bonus you keep:				$1,226.00
Total monthly gross income				$1,375.00

7-D

[55] Amway distributors use this technique in recruiting new distributors. (Yager, CX 1040-U; Trozera, CX 1031-E; Cliett, Tr. 3758-59) In 1977, Amway raised the basic amount to be used in the circles to $250. (RX 401, pp. 7-8)

136. In speaking to a new Direct Distributors meeting in June of 1974, Mr. Van Andel explained the reasons for specifying a particular sum to represent the amount of the distributors' sales in the circles drawn to show the plan (CX 1041-T):

> What is my personal opinion with regard to the $200 circles versus the $100 circles? Well, we think that the $200 circle concept raises the, the vision of people, and we have found through experience, as you have I'm sure, that people tend to do that which you ask them to do. If you had $50 circles, they'd probably do $50. If you have a hundred they do a hundred, and if you do $200 they probably do $200. Now, there's a limit to that, and, er, you know, you can follow that through and say let's make 'em $5,000 circles — well, it doesn't quite work out that way. But I think the general consensus, and we discussed this widely with Direct Distributors, Diamond Direct Distributors, with the ADA Board, was that the $100 figure was too low. And that by raising it to $200, it would result in a general upgrading of the potential of a great many distributors, which would be good for them and good for you. And that's, I think, about the way it's worked out for most people. . . .

137. The average monthly BV of Amway distributors in fiscal 1969-70 was about $20 a month. In fiscal 1973-74 the average BV for each distributor was about $33 a month. (CX 517-F, Z-95) Much of this amount is consumed by the distributors themselves rather than resold. The distributors obtain Amway products with about a 30% discount off the retail price. Many of them consume large amounts of the products every month. (Cook - $75, Tr. 4742; Marshall - $35 to $45, Tr. 4761; Woodworth - $60, Tr. 4787; Wespinter - $75 to $100, Tr. 4884; Rivett - $60, Tr. 4971; Nieman - $75 to $100, Tr. 5081; Hendrickson - $150, Tr. 5181; Gregory - $40, Tr. 5209; Williams, $125-$150, Tr. 5325; Evans - [56] $70-$80, Tr. 5300-01; Wakeman - $30-$40, Tr. 5446; Burgess - $25-$40, Tr. 5460; DeJean - $30-$40, Tr. 5501; Wong - $80-$100, Tr. 5650; Wolfe - $100, Tr. 5664)

138. Amway instructs new distributors to recruit additional distributors by the following method. After making a list of friends, relatives and neighbors, the new distributor is instructed (RX 331, p. 1-D):

> Give these friends, relatives and neighbors the benefit of a full presentation of the Amway Sales and Marketing Plan. Don't try to explain over the phone. Encourage them to attend the meeting by telling them that this is an opportunity to be in business for themselves on a part time basis with no investment in inventory necessary. Tell them they may build a business earning as much as $1000 or more a month. Mention that you have started your own independent business on a part time basis and that you would like to tell them about it.

Amway distributors use this technique in recruiting new distributors. (Dirksen, Tr. 423; Holdridge, Tr. 743, 819; Bernard, Tr. 1364–65, 1376–77; Johnson, Tr. 1439; Rovena, Tr. 1633–34; Blinko, CX 1041–Y; Johnson, CX 1115–B; Williams, CX 990–Z–30; Eldridge, CX 999–V)

139. Amway recruiting literature used in 1964 stated that: "Sponsoring is easy!" The 29 page single spaced manual continued, however, to outline the method used in sponsoring, referring to several other Amway manuals, and concluding: "After your first reading this manual may seem a bit confusing to you. If (sic) may seem like there are a tremendous number of things to remember and learn. Don't try to remember all the details now. Start with the first step . . . ." (CX 89) (1964) More recent recruiting literature is even more detailed. (CX 91) (1975) [57]

140. Amway literature explaining the Sales and Marketing Plan cautions that distributors incur expenses in the operation of the distributorship, such as automobile, telephone, stationery, literature, utility and other operating expenses. (CX 88, p. 10, RX 401, p. 10, CX 87, CX 62–Z–18, CX 60–Z–19, CX 61–Z–18, CX 91–H, CX 1096, pp. 2–H and 3–H, CX 793, p. 10) Distributors are also told at meetings to watch expenses. (DeVos, CX 1045–B)

141. Amway has warned its distributors that it is realistic to expect a new distributor to drop out in only one week. (CPF 505) In 1970, Mr. DeVos told new Direct Distributors that "about half the people who sign up the first time sign up the second year." (CX 1045–B) Amway teaches its distributors to expect newly sponsored distributors to quit the business and to be prepared for the let down. (CX 1000–W) [58]

Pyramid Sales

142. "Pyramid" sales plans involve compensation for recruiting regardless of consumer sales. In such schemes, participants receive rewards for recruiting in the form of "headhunting fees" or commissions on mandatory inventory purchases by the recruits known as "inventory loading." (Van Andel, Tr. 1820–21; Patty, Tr. 3147, 3091–92; Cady, Tr. 5778–79)

143. "Pyramid" sales plans based on inventory loading or headhunting fees create an incentive for recruiting rather than selling products to consumers. This potentially results in the number of recruits outgrowing the market for products being sold to consumers. (Granfield, Tr. 2996–97)

144. The Amway Sales and Marketing Plan provides incentives for sponsoring which are based on sales of products to consumers.

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(Van Andel, Tr. 1823–24; Granfield, Tr. 2951–52; Patty, Tr. 3092–95; Cady, Tr. 5779–81; Max, Tr. 5995–97) It is not a pyramid sales plan.

145. Amway's buy-back rule deters inventory loading by sponsoring distributors. (Van Andel, Tr. 1999–2000; Halliday, Tr. 6231–32; S. Bryant, Tr. 4062–63)

146. Amway's 70% rule deters inventory loading by sponsoring distributors. (Cady, Tr. 5795–97; Halliday, Tr. 6231; Lemier, Tr. 176)

147. Amway's ten customer rule deters inventory loading by sponsoring distributors. (Max, Tr. 5996–97) [59]

Saturation

148. Distributors have come into the Amway business in the United States as follows (RX 381):

Year	*New Distributors*
1972	255,000
1973	231,000
1974	213,000
1975	237,000
1976	280,000

Each Amway distributor who wants to continue as an authorized Amway distributor (except those recruited after August 31 of that year) must notify Amway. At the end of the calendar year the files are cleared of the names of distributors who elected not to continue. The number of distributors at the beginning of the year therefore is close to the number of active distributors. (Halliday, Tr. 6483–87) The turnover rate for all Amway distributors (including international) is as follows (RX 383):

Year	*Number at the End of Prior Year*	*Number at beginning of Year*	*Turnover*
1972	646,633	320,738	50.4%
1973	655,310	306,002	53.3%
1974	546,328	298,561	45.4%
1975	518,583	294,328	43.2%
1976	549,516	315,187	42.6%
1977	610,059	359,470	41%

149. Amway distributors from various parts of the country gave credible testimony that they have found that in recent years it has become easier to sponsor new distributors. (Hansen - Grand Rapids, Michigan, Tr. 3271–72; Cliett - Fairfax Station, Va., Tr. 3747; Zizic - Timonium, Maryland, Tr. 4113–14; Hunt - Holly Pond, Alabama, Tr. 4412; Wespinter - Portage, Michigan, Tr. 4883–84; Evans - Wray,

Colorado, Tr. 5263-64; Lamb - Missoula, Montana, Tr. 5607; Case - Phoenix, Arizona, Tr. 3401-02) [**60**]

150. The Amway Sales and Marketing Plan, not being a "pyramid" plan, has not led to any significant difficulty in recruiting new distributors.

a. Some witnesses, called in support of the complaint, testified to their difficulty in sponsoring new distributors in their areas of the country. Other evidence, however shows that the opportunity to sponsor new Amway distributors has continued in those areas:

Baton Rouge, Louisiana - The new distributors increased from 332 in 1975 to 547 in 1976. (RX 372) The population increased 45,000 from 1970 to 1976. (RX 354)

Charlotte, North Carolina - The new distributors increased from 688 in 1975 to 1014 in 1976. (RX 375) The population increased 65,000 from 1970 to 1976. (RX 357)

Conway, South Carolina - The time period for which there was testimony about difficulty in sponsoring (1973-1976) shows a slight drop in new distributors in 1973 from 326 to 307 in 1976; the total number of distributors increased from 536 in 1973 to 678 in 1976. (RX 376) The population increased 22,000 from 1970 to 1976. (RX 358)

Florida counties - Although the total number of distributors has declined from 1971 through 1976, there have been an average of over 2,000 new distributors added each year during this time. (CX 898-A, RX 378, RX 379, RX 380) The population has increased 620,000 from 1970 to 1976. (RX 361-63)

Dallas/Ft. Worth, Texas - Although there was a 64% decrease in the number of new distributors recruited from 1971 to 1973, the number increased by 56% from 1973 to 1976. (RX 377) The population increased 175,000 from 1970 to 1976. (RX 359) [**61**]

Kalamazoo, Michigan - The population increased 13,000 from 1970 to 1976 (RX 355) and there were an average of 775 new distributors in each year from 1972 to 1976. (RX 373)

b. Other witnesses whom I heard and find credible were called by respondents and testified that in several of these areas they had no difficulty sponsoring new distributors during the relevant time. (Rivett - Baton Rouge, Tr. 4943-44; Gregory - Dallas/Ft. Worth, Tr. 5200-01; Wespinter - Kalamazoo, Tr. 4882-84; Brown - Florida counties, Tr. 4997-5001)

151. It is relatively unlikely that the available supply of potential Amway distributors will be exhausted in any particular area. It is predominently a part-time activity. The population of the country continues to grow. Former Amway distributors sometimes come back in the business. (Max, Tr. 5950–52; RX 381) Twenty-five percent of the population move every year. (Van Andel, Tr. 1829–30, 1916) Only one-fourth of all Amway distributors engage in sponsoring (Van Andel, Tr. 1828–30), and there has been no decline in the percentage of Amway distributors who sponsor over the last five or six years. (Max, Tr. 5958–59, 5965–69; RX 415) Amway's sales trend has shown almost uninterrupted growth (RX 448) in each state as well as nationally. (RX 432) Average monthly income for Amway distributors has been increasing. (Cady, Tr. 5818) Average sales per distributor have been increasing. (Max, Tr. 5965–69) There has been an increase in the number of Direct Distributors. (CX 896)

152. Amway has had a rule against distributors misrepresenting the Amway Sales and Marketing Plan as involving only sponsoring. Amway enforces this rule by terminating distributorships or by censure, impounding bonuses and reorientation. (Halliday, Tr. 6488–97) [**62**]

Direct Selling

153. Direct selling companies distribute their products through independent salespersons who sell to consumers person-to-person on a commission basis, typically demonstrating the effectiveness of the products in the homes or places of business of the customers. Some direct selling companies are "multi-level," with independent distributors acting as wholesalers as well as retailers. Others are integrated down to the wholesale level, with only the retail sales to consumers being made by independent salespersons. (Van Andel, Tr. 1691–95; Granfield, Tr. 2917–18)

154. There are in the United States more than 2000 companies engaged in direct selling. (Van Andel, Tr. 1812, 1693–95; RX 403) There are about 30 to 40 major direct selling companies in the United States. (Patty, Tr. 3067) Direct selling industry sales annually amount to between ten and fifteen billion dollars, about one or two percent of all retail sales. (Patty, Tr. 3068) This does not include companies selling such products as insurance, real estate, milk or newspapers. (*Ibid.*) Direct selling companies hire about two million people. (Patty, Tr. 3069) Avon is the largest direct selling company with annual sales of $1.25 billion. (Van Andel, Tr. 1693) Many direct selling companies have been acquired by large companies not previously engaged in direct selling. Some of these acquired compa-

nies include Tupperware, Electrolux and Fuller Brush. (Patty, Tr. 3146)

155. Direct selling often starts with the salesperson calling on friends and relatives but to build a business eventually requires calling on strangers. (Patty, Tr. 3088) Door-to-door selling is direct selling by knocking on strangers' doors, although the term has a broader definition meaning direct selling of all types. Amway advises its distributors to sell to friends, relatives, neighbors or persons referred by a customer. This gives the distributor an introduction to the prospect. (Van Andel, Tr. 1757–58) **[63]**

156. Direct selling companies usually sell high quality products, in order to recruit salespersons and to induce homeowners to allow sales persons into the privacy of their homes. The products typically are high priced items such as encyclopedias and vacuum cleaners (where the salesperson can make up for demonstrating lost sales through the high price of products sold) or low priced, frequently purchased items where the salesperson is trying to develop a regular clientele. (Patty, Tr. 3080–81) Some companies sell an expensive high quality line of products through direct sales and a different inexpensive line through retail stores. (Patty, Tr. 3102) One encyclopedia company (World Book) tried selling through a department store but found very few people would pay for the books without personal selling and demonstration afforded by direct selling. (Patty, Tr. 3102–03)

157. Direct selling provides convenience for consumers who have to travel long distances to shop or who may be confined to their homes by age or health or a number of small children. It provides product demonstration not available in retail stores. Direct selling also provides supplemental income for many people working part-time. (Patty, Tr. 3075–77) It also allows the salespersons to be their own bosses. (Patty, Tr. 3090)

158. Direct selling can provide a manufacturer with distribution of a new product without heavy media advertising and promotion costs. (Granfield, Tr. 2944–45; Patty, Tr. 3069–75)

159. Selling through independent distributors avoids fixed costs incurred by selling through employees, such as social security, unemployment compensation and employment salaries. (Granfield, Tr. 2932) **[64]**

160. Successful direct selling usually requires:

(a) Dependable, quality products. (Granfield, Tr. 2950; Patty, Tr. 3083) A quality product makes it easier to recruit distributors. (Cady, Tr. 5765–66);

(b) Money-back guarantee. (Granfield, Tr. 2950) An unconditional guarantee helps recruit distributors by assuring them of the quality of the product and encourages consumers to try a new product. (Cady, Tr. 5769–70);

(c) Ability to recruit, retain, train, and motivate a sales force. (Granfield, Tr. 2938–41; Cady, Tr. 5773–74; Patty, Tr. 3081).

161. Direct selling provides a channel of distribution for a relatively small or new company which has new, good products but does not have the financial resources to sell in traditional retail stores, with the high advertising and other expenditures entailed by that method. Lack of financial strength in such circumstances leads to the small innovative company being acquired by larger companies. (Patty, Tr. 3074)

162. Annual turnover of salespersons for companies engaged in direct selling of lower priced products averages about 100%. (Granfield, Tr. 2942–43; Patty, Tr. 3106) A direct selling company with less than a 60% turnover rate is doing a relatively good job of recruiting and retaining salespeople. (Patty, Tr. 3106–07)

163. Amway's annual turnover rate has usually been in the 50% to 60% range. (RX 383) [65]

164. Because of the relatively high rate of turnover among salespersons, direct selling companies continually recruit new salespersons. (Patty, Tr. 3103–04; Cady, Tr. 5778) Recruiting is essential to a direct selling company. (Patty, Tr. 3103)

165. Some direct selling companies use employees to do most of the recruiting of new salespersons. Independent contractors do the selling, and may be paid a small reward for referring a new recruit. Avon, Electrolux and greeting card companies use this system in the United States, although overseas Avon and Fuller Brush use the same system of recruiting as Amway. (Patty, Tr. 3153; Van Andel, Tr. 1695, 1889; Granfield, Tr. 2959–60)

166. Amway pays about 60% of its sales dollar to distributors in payment for the distribution of Amway products. (Halliday, Tr. 6213–14) Distributors for other direct selling companies do not get paid any more money, if they get as much. (Halliday, Tr. 6191–93)

167. "Multilevel direct selling" refers to a firm which has a number of levels of supervision, which involve independent contractors who are not employees of the company. They are compensated on the basis of margin rather than a commission or salary. Several direct selling companies are multilevel, including most encyclopedia companies. (Patty, Tr. 3130–32; Van Andel, Tr. 1694–95)

168. Some multilevel direct selling companies have engaged in

"pyramid selling," involving "inventory loading" and "headhunting" fees. These companies have a large inventory requirement for a new distributor, and reward distributors for bringing into the business a new distributor. The result emphasizes recruiting of new distributors rather than selling the products to consumers. Typically, these pyramid companies require new recruits to buy $2000 to $5000 in inventory, with as much as half of that amount going to the recruiting distributor. (Patty, Tr. 3091–92) **[66]**

Amway's Product Markets

169. Amway started in the business of manufacturing and distributing soap and detergents, and this still is its primary activity. (Van Andel, Tr. 1680–81) Soap and detergents accounted for more than 40% of Amway's 1974 sales; polishes and sanitation goods accounted for 20%; and toilet preparations accounted for about 7%. (RX 405) Amway's 1974 sales of soap and detergents amounted to $57.9 million, accounting for 1.7% of the total sales of soap and detergents in this country. (RX 404; RX 406)

170. The market for soap and detergents in the United States includes laundry detergent, dishwashing detergent (either of which may be liquid or powder), bar soap, and a small volume of speciality products such as laundry aids and scouring cleansers. (Diassi, Tr. 5517, 5558)

171. The manufacturing and distribution of soap and detergents is highly concentrated, with the largest firm, Procter & Gamble Company, accounting for half the sales. Procter & Gamble, Colgate-Palmolive Company and Lever Brothers account for 82% of industry sales. The fourth largest firm, Purex Corporation, has 4% of sales. (RX 407; Diassi, Tr. 5516–17; Robbins, Tr. 6744) Market shares in the laundry detergent industry, in pounds produced in 1973 and 1975 were (CX 561-G):

	1973 % of Market	*1975 % of Market*
Procter & Gamble		
Tide	26.0	28.0
Cheer	8.5	8.5
Bold	4.5	4.5
ERA		4.5
Six Others	14.0	10.0
Total P & G	53.0	55.5

[67] Lever		
All-Liquid	1.1	1.5
All-Powder	6.5	6.5
Wisk	5.1	6.0
Breeze	2.4	2.4
Three Others	6.9	5.2
Total Lever	22.0	21.6
Colgate		
Fab	5.5	4.8
Cold Power	4.0	4.0
Ajax	3.0	3.0
Dynamo	0.7	2.0
Two Others	2.0	1.9
Total Colgate	15.2	15.7
Others	9.8	7.2
Total	100.0	100.0

Amway's leading product, SA8 Plus, accounted for .78% of this market. (CX 561-F)

172. The personal care products market is also concentrated. The largest firm, Procter & Gamble, has 24% of total sales. The next three, Lever Brothers, Colgate-Palmolive and Gillette, account for 25%. (RX 408)

173. Procter & Gamble Company has been in the soap business since 1837 and had 1976 sales of about $6.5 billion. Colgate-Palmolive Company started in the soap business in 1864 and had 1976 sales of about $3.5 billion. Unilever Ltd., known as "Lever Brothers" in the United States, started in the soap business in 1894 and had 1976 sales of 8.7 billion pounds sterling. (RPF 50) Two other companies manufacture and distribute some of their brands of soap and detergents nationally, Purex Corporation and Church and Dwight Company (using the "Arm & Hammer" label). (Robbins, Tr. 6718-19; Diassi, Tr. 5571-72) [68]

174. Private label soap and detergents are manufactured by a few relatively small companies and are sold by retail stores under their own brand names. Total national private label sales amount to about 5% of the detergent market. (Diassi, Tr. 5519-20, 5548)

175. The three largest manufacturers in the soap and detergents industry spent over a half a billion dollars in advertising and sales promotion in 1975. (RX 410-13) Procter & Gamble, the nation's

largest advertiser, spent over $360 million in product promotion in 1975. (RX 413) Amway spent less than a million dollars in that year for institutional (non-product) advertising. (Teska, Tr. 2751–52; RX 413)

176. Most Amway products are of the kind sold through chain food stores. (Cady, Tr. 5758) Over 95% of the retail sales of soap and detergents in this country is by grocery stores. (Diassi, Tr. 5576; Cady, Tr. 5758) Obtaining retail shelf space is critical for successful entry into the soap and detergents market. (Cox, Tr. 3819) Retail grocery stores are reluctant to add a new product unless it promises to sell quickly. (Diassi, Tr. 5535) The successful marketing of a national brand of detergent through retail stores requires that the product be available in almost every retail outlet where detergents are sold. (Diassi, Tr. 5525–26) Retail grocery chain stores are becoming increasingly concentrated. (RX 449, pp. 9–11)

177. Attempted new entry into the soap and detergents market has faced substantial increased promotional and advertising spending by Procter & Gamble. (Max, Tr. 5930–32; Robbins, Tr. 6728–30; Dunlap, Tr. 6683) Procter & Gamble also counters attempted introduction of a new brand of detergent with introduction of its own new brand. (Robbins, Tr. 6731–32; Cox, Tr. 3854–55) By producing many brands, Procter & Gamble has succeeded in occupying a great deal of grocery shelf space. (Cox, Tr. 3819) **[69]**

178. The three largest manufacturers of soap and detergents at first resisted the demand for non-phosphate detergents during the early 1970's, brought about by concern with the environmental impact of phosphate detergents. (RX 353) Several companies attempted to make and sell a non-phosphate detergent. (Cox, Tr. 3806–07) Armour & Company, established in 1863 with 1976 sales of $2.7 billion, and an established firm in the bar soap industry, attempted to enter the laundry detergent market with a concentrated non-phosphate product called "Triumph." Despite considerable promotion, the attempt was a failure. (Diassi, Tr. 5527–30) Church & Dwight ("Arm & Hammer") entered the market with a non-phosphate laundry detergent and gained about 4% of the market and was the only successful entrant with a non-phosphate detergent. Church & Dwight is one hundred years old and was already in grocery stores with an established brand of washing soda and baking soda. (Diassi, Tr. 5571–73) Following this entry, and following ecology legislation by several state and local governments, the major soap companies started selling non-phosphate detergents. (Diassi, Tr. 5570)

179. Purex Corporation started manufacturing household bleach in 1927. Purex started manufacturing dishwashing detergent in 1947

and laundry detergent in 1952. Since then, Purex has been able to sell several of its soap and detergent products nationally, using established trademarks gained through acquisition ("Old Dutch Cleanser," "Brillo," "Sweetheart" soap), some national advertising, its own sales force, and prices about 20% below those of the major soap and detergent companies. (Robbins, Tr. 6696, *et seq.*)

180. Los Angeles Soap Company has been marketing soap through retail stores for 116 years, and has been using the "White King" tradename since the turn of the century. It sells regionally in 18 western states, where it has 2% of the market, and prices low enough to allow the grocer to double and sometimes triple the profit he would make selling national brands. (Dunlap, Tr. 6640–42, 6653–54, 6670) In the early 1960's, Los Angeles Soap Company tried to enter the eastern market with a plant at Framingham, Massachusetts. The expansion failed and the plant was sold as scrap. (Dunlap, Tr. 6671–72) [70]

181. Except for the non-phosphate detergents, there has been virtually no new successful entry in the national market for sales of soap and detergents through retail stores in the last thirty years. (Cox, Tr. 3799, 3805; Diassi, Tr. 5523–33; 5571–72; Granfield, Tr. 2936–37; Dunlap, Tr. 6670–72, 6676–77) The market has been increasing at a rate of about 4% a year since 1954. (Cox, Tr. 3807)

182. Amway's laundry detergent sells at retail for slightly more per use than the detergents of the major soap and detergents companies, and slightly less if Amway's large size product is purchased. (Max, Tr. 6038–45) On a cost per use basis, in 1967, SA8 was less than 3¢ and Tide was about 7¢. At this time, SA8 use direction was 5/32 cup per washload and Tide was 1.75 cup. The cost per use drew close in 1968 when the use direction was changed: SA8 1/4 cup and Tide 1.25 cup. In 1972, Tide again changed its use direction to 1 cup per washload, in response to "phosphate down the drain" legislation. (CX 561–Z–11 - 12) Since then SA8 has cost about 1¢ to 2¢ per use more than Tide and the other leading laundry detergents. Sold in the large size (100 lbs.), however, SA8 has a lower per use cost than any laundry detergent. (CX 561–Z–14) In 1973, Amway introduced SA8 Plus, selling at retail for about the same as SA8, but apparently superior in cleaning power to either SA8 or Tide. (CX 561–Z, Z–3 to Z–4) And, unlike detergent purchased at the grocery store, Amway's products are delivered to the consumer's home. (Max, Tr. 6045)

Amway Is a Substantial Industrial Company

183. Amway's United States sales have grown from $4.3 million

in 1963 to $169.1 million in 1976. Worldwide sales of Amway products in 1976 amounted to about $205 million. (RX 431, RX 448) [71]

184. Amway employed over 1,500 persons in 1976 at its plant in Ada, Michigan, with an annual payroll of $19 million. The plant represents a capital investment of $56 million. In 1976, Amway paid over $60 million to its distributors, over $41 million for raw materials, and $11 million to third parties for transportation of Amway products. (RPF 248)

185. All but a few of the regular-line products sold under the Amway name are manufactured by Amway or its subsidiary, Nutrilite Products, Inc. (Van Andel, Tr. 1805) Amway's plant and equipment are modern and efficient. (RX 68 to RX 277) Amway follows recognized industry standards of good manufacturing practice. (RPF 90) It has a substantial research and development operation and expends generally as much per sales dollar as larger competitors in the personal care products field. (RPF 86)

186. Amway's products have very high consumer acceptance. A market study in the record shows that of 37 brands of laundry detergent, Amway's product, with only a very small market share and no national advertising, was third in brand loyalty. (Cady, Tr. 5823) Amway's dishwashing liquid soap led all 16 brands surveyed in consumer acceptance. (Cady, Tr. 5819-22) In each of the markets for automatic dishwasher detergents, detergents for fine clothing, bleaches, rug cleaners, and laundry additives, Amway's products were second in brand loyalty. (Cady, Tr. 5822) Professor Cady, a marketing specialist from the Harvard Graduate School of Business Administration, testified that (Tr. 5823):

> What this means overall is that consumers are obviously well served by the products that Amway supplies them with. In fact, they are so well-served, in the face of a large number of available substitutes, they purchase Amway products to a degree which is almost unknown to other brands in the market.

[72] Amway has achieved this consumer acceptance for its products while having no more than 1.7% of any market in which it competes (RX 406) and while spending a total of about two million dollars for advertising and sales promotion for the years 1972 through 1975, while its top five competitors were spending about 2.3 billion dollars for that purpose. (RX 410 to RX 413)

187. Amway, through its distributors, provides services to consumers not readily available when products are purchased at a retail store. Amway has a 100% money-back guarantee which permits a customer who is not satisfied with an Amway product to return it with the choice of replacement, repair, credit, or refund of full

purchase price (RPF 93, 94, 98) Distributors provide the service of home or commercial delivery at the time convenient to the customer, including weekends and evenings. (RPF 98(a)) Amway ditributors demonstrate and explain product use. (RPF 98(b) and (c)) Distributors perform water hardness tests and recommend the use of a dishwashing detergent for hard or soft water. (RPF 98(d)) Amway and its distributors provide advice for safe product use. (RPF 98(e), 98(i)) Distributors leave sample products with customers for trial use before purchase. (RPF 98(f)) Distributors install Amway products when necessary, such as smoke detectors, and deliver to the laundry room 100 lb. and 85 lb. boxes of detergent. (RPF 98(m)) **[73]**

DISCUSSION

The following discussion is intended to summarize and supplement the foregoing findings of fact and to present conclusions of law derived from the facts as found.

Summary

Amway was founded in 1959 by Jay Van Andel and Richard M. DeVos, who continue as its principal executives and stockholders. Prior to that time, they sold Nutrilite food supplements door-to-door and headed a large group of distributors. They began having supply problems and started looking for different products to sell. They looked for readily consumable, low-priced, repeat sale products which would be different than those found in retail stores.

Mr. Van Andel and Mr. DeVos started distributing a liquid biodegradable detergent[5] which they named "LOC." A few months later, they acquired the small manufacturer of LOC, moved the assets to Ada, Michigan, and started manufacturing their own products under the Amway label. Amway's second product, also biodegradable, was a powder laundry detergent, SA8. Amway continued to introduce new products and now manufactures and sells more than 150, but its main product market continues to be soap and detergents, accounting for more than 40% of sales. **[74]**

Amway's principal products are of the kind that are sold in chain food stores. These markets are dominated by a few large manufacturers, of which the largest is Procter & Gamble. Procter & Gamble sells about half of all of the soap and detergents sold in this country, and one-fourth of the personal care products. The three largest firms

[5] Synthetic detergents have largely replaced soap for laundry and dishwashing purposes in the last 30 years, being chemically different and much more effective. (Diassi, Tr. 5573-74) "Biodegradable" means that the ingredients of the detergent are broken down by natural biological action, helping to eliminate foaming problems in lakes and streams. (Halliday, Tr. 6095, 6154)

in the soap and detergents market sell over 80% of total market sales and this dominance existed prior to Amway's origin. *FTC* v. *Procter & Gamble Co.,* 386 U.S. 568, 572–73 (1967). Entry into this market has been blocked for thirty years by the major soap companies by product differentiation achieved through advertising, by retaliatory pricing and promotions, and by brand proliferation.[6]

Amway entered the market with biodegradable detergents. Mr. Halliday, an officer of Amway, was asked (Tr. 6154):

Q. At the time of introduction of LOC and SA-8 by Amway, do you know whether other detergents were then biogradeable [sic]?

A. I know that none of the detergents marketed by the big three soapers were or did contain biodegradeable ingredients at that time.

Q. How long afterward did the detergent industry essentially go biodegradeable?

A. It was up to 10 years afterwards.[7]

[75] Amway marketed its products by selling directly to consumers in their homes through a large number of salespeople. These independent distributors find the customer, and explain, demonstrate and deliver the products. Most of them work part-time. Three out of four quit after the first year.[8]

Some promoters posing as direct selling companies have rewarded recruiting itself in "pyramid" plans, involving "headhunting" and "inventory loading." Recruits earn money by securing further recruits, and there are few product sales to consumers. In order to recruit an effective sales force, Amway encourages its distributors to sponsor new distributors. This is not, however, a pyramid plan. In the Amway system, the incentive to recruit comes from the commission distributors receive on product sales by sponsored distributors in their organizations. But, by several rules, Amway requires that commissions are not paid unless the products are sold to consumers. Distributors must each sell to ten retail customers every month; the distributors must certify that 70% of the products purchased by them during the month have been resold; and inventory loading is further deterred by a rule requiring distributors

[6] To some extent the effect of these practices on consumers has been mitigated by the growing concentration and power of food chains and their tendency of using soap and detergents as loss leaders. (Diassi, Tr. 5534; Finding 176)

[7] In typical oligopolistic conduct, the major soap companies were slow to react to public demand for non-phosphate detergents in the early 1970's, allowing successful entry by at least one manufacturer selling through food stores. (Finding 178)

[8] Amway's turnover rate among distributors is better than most direct selling companies. (Findings 148, 162–163)

to buy back the inventory of any of their sponsored distributors leaving the business.

Amway has successfully entered the soap and detergents market because its distributors sell directly to consumers in their homes or businesses, rather than through retail grocery stores. Amway has achieved this method of distribution through several restraints on its distributors, including the retail store rule, the cross-group selling rule, and regulation of its distributors' advertising. These are reasonable vertical restraints. However, respondents went too far in controlling intrabrand competition while promoting interbrand competition. In addition to the beneficial restraints, respondents also stopped Amway distributors from competing among themselves for customers and fixed the prices at which Amway products are sold among distributors and to consumers. [76]

Distributor Restraints Are Vertically Imposed

The theory of the complaint anchors on the alleged horizontal nature of restrictions imposed on Amway distributors. Complaint counsel argue that the Amway Distributors Association is:

> [R]un by a clique of the most successful Amway Distributors. It exists for the sole purpose of protecting the interests of the successful from the hoards of competitors and newcomers who enter the distribution stream daily. Its mission is protection and its clout is termination. The Association is the root cause of all of the Section 5 violations, including the very existence of the Amway Sales and Marketing Plan. (CB, p. 3)

Complaint counsel state that about 35 Nutrilite distributors, including Mr. Van Andel and Mr. DeVos, decided collectively (1) that they needed a product, found one called "Frisk," and (2) that the "Marketing Plan" with its restrictions should be imposed on distributors. The uncontradicted testimony of Mr. Van Andel tells a different story. He testified that the Nutrilite distributors started having problems with their suppliers in 1959. (Van Andel, Tr. 1673–76):

> At that time, in order to attempt to bring this intramural fight to a conclusion and arbitrated, if you wish, a small group of distributors were appointed, of which I became the chairman, to try to work with both companies and try to work out an arrangement that would bring peace and tranquility back. [77]
>
> The arrangement to do this was not entirely successful. I met many times with the principals of both companies and this arrangement culminated in an offer by one of the companies to me to become president of their company. Mr. DeVos and I discussed this in some detail and we realized that the inherent problems were not being solved because it appeared to us the inherent problems were with the people who owned

those companies and that those problems would continue regardless of who managed them.

It appeared to us therefore the Nutra-Lite [sic] structure, the companies behind the Nutra-Lite distributing organization were in great danger of collapsing, that the time and effort they were putting into fighting amongst themselves instead of competing in marketplace would eventually destroy the company. Therefore it appeared to us if we were going to survive in business, if we were going to be able to continue and have some return on our 10 years of effort, it would be best if we would go into business ourselves, producing our own products and selling them through our own sales organization and controlling the entire distribution and manufacturing operation.

This then necessitated a very careful change in the distributor organization that we had built, which had been very strongly built with an allegience to Nutra-Lite food supplement as a product to sell. The Nutra-Lite organization as well as the Amway organization is built entirely of volunteers, people who voluntarily are distributors and it is very important if you are going to go into a different direction that the volunteers follow. They don't have to. They could all quit. [78]

So it was very necessary for us, we felt, to get their concurrence that our plans were good ones and that they would continue with us.

In order to do this, we felt we had to communicate with them very closely, and that at that time we put together a structure which I think you are familiar with, called Amway Distributor Association.

That association at that time was called the American Way Association; its name was changed later.

Its primary purpose was to attempt to communicate and hold together what business we had until we could shift gears and develop our own manufacturing operation, develop our own products and continue on.

This was basically the genesis of the Amway Corporation and we began with one or two products and continued on until where we are today.

Q. Did the American Way Association, when it was formed, have any particular products to distribute through the organizations of its members?

A. The American Way Association was never developed to be a product distributing structure. Rather it was in the nature of an association of independent contract or [sic] business people whereby they would have a means of formalized communication with Mr. DeVos and myself who proposed to set up the product distribution and manufacturing operation.

We developed a system whereby a board of directors of the association could be elected, a system whereby we could meet with them from time to time and discuss our plans and communicate with them and hopefully get them to agree to continue with us. [79]

Q. Did the association or did the association members determine a particular product that would be distributed through its organizations?

A. The association members were polled by us and asked by us if they were interested in having us supply certain products.

Q. "Us," meaning yourself, Mr. DeVos?

A. By "us" I should say, Amway Corporation, Mr. DeVos and myself and the company that we built behind that.

Two of the 35 former Nutrilite distributors who became Amway distributors were called as witnesses. Walter Bass, the first president of the ADA, acknowledged that Mr. Van Andel and Mr. DeVos created Amway. He was asked about the formation of Amway and the ADA. (Bass, Tr. 70-71):

Q. Were Richard DeVos and J. Andel [sic] some of the key people involved?

A. They were the key people.

Q. They were more key than any other persons, that is what you are saying?

A. It was their idea.

Q. Were they doing business under the name Ja-Ri Corporation?

A. Yes.

Q. For what reason, if you know, did these key people, yourself included, get together to form this association?

A. We foresaw some problems in the Nutra-Lite organization that alarmed us and rather than to allow is [sic] to just go out of existence, the idea of Amway was developed.

[80] Mr. Bass could name only 6 of the 35 Nutrilite distributors who allegedly started Amway. (Bass, Tr. 68-69) Bernice Hansen, also one of the 35 Nutrilite distributors who became Amway distributors, was called. She too identified Mr. Van Andel and Mr. DeVos as the persons who "started Amway." (Hansen, Tr. 3301-02)

The impetus for the restrictions imposed on distributors in this case clearly came from above. Mr. Van Andel and Mr. DeVos started Amway, not the 35 Nutrilite distributors. Mr. Van Andel and Mr. DeVos used the association of distributors to communicate and control the distribution of the products they were to make, but the thrust to build the Amway organization as it now stands came from those two individuals, not from a committee. (Findings 19-25)

Here the dealers do not control the manufacturer, as in *United States* v. *Topco Assoc., Inc.,* 405 U.S. 596 (1972) and *United States* v. *Sealy, Inc.,* 388 U.S. 350 (1967). Nor did the dealers here prevail upon the manufacturer to impose the restrictions. *United States* v. *General Motors Corp.,* 384 U.S. 127 (1966). Mr. Van Andel and Mr.

DeVos initiated and orchestrated the scheme, and notwithstanding the willing participation of the distributors, Amway is the dominant partner. *Newberry* v. *Washington Post Co.,* 438 F. Supp. 470, 474 n.5 (1977).

When Amway was created, Mr. Van Andel and Mr. DeVos, through the Ja-Ri Corporation, were distributors as well as manufacturers. (CX 53-J) But in replacing the previous suppliers in the Nutrilite organization, and adopting the distribution system from that organization, they were acting essentially alone.[9] The restraints are not, therefore, "primarily 'horizontal.' " *The Coca-Cola Company,* Dkt. 8855, Commission Opinion p. 8 (Decided April 7, 1978). [81] "[O]nly by ignoring the essential relationships which exist" between Amway and the distributors might it be concluded that the restraints are horizontal. (*Ibid.*)

Horizontal Cooperation by ADA

Complaint counsel argue that respondents are engaged in an unlawful group boycott because the ADA is the "final arbiter of disputes and interpretations of the Code of Ethics and Rules of Conduct." (CB, p. 5)

The Amway Distributors Association of the United States is a voluntary association of independent Amway distributors. (Findings 11-12) Voting membership in this trade association is open to qualified Direct Distributors. (Finding 13) Voting members may attend annual meetings to receive reports concerning Amway and elect ADA Board members. (Finding 76)

The ADA Board meets four times a year. Amway seeks advice from the ADA Board concerning any changes in Amway rules. (Finding 78) Rather than an agreement among equals, this aspect of the ADA is a means by which Amway controls the distribution of its products through independent salespersons by convincing them—not coercing them—to accept changes in the Amway Sales and Marketing Plan. Mr. Halliday testified that (Tr. 6612-13): [82]

> As a matter of policy, Amway Corporation presents the proposals for changes of rules to the board for educational purposes, instructional purposes, for feedback from the board as representative of the distributor organization as to the kind of reaction to the change, as to the timeliness of implementing the rule changes; it is an opportunity to sell the board so that they and their distributors in their organizations wil enthusiastically support the notion of moving ahead in that direction. Again, we ar talking about a group of volunteers.

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[9] There is some evidence that one of the distributors suggested to Mr. Van Andel and Mr. DeVos that t product "Frisk" be distributed. (Halliday, Tr. 6541) The preponderance of the evidence, however, supports t finding that the genesis of Amway was vertically imposed. *Cf. Sandura Company* v. *FTC,* 339 F.2d 847, 857-58 ((Cir. 1964).

You just don't say tomorrow we are going to propose a new rule and bang this is the rule, or tomorrow we are going to change a rule and bang this is the rule. What we try to do is to present it to the board and the distributor organization [so] that when the date of implementation occurs, which we determine, that it is accepted with full enthusiasm and that people move ahead voluntarily, then, to act in accordance with those changes.

The ADA Board of Directors also acts as an arbitration panel for disputes in which Amway decides to discipline a distributor for a rule violation. If Amway decides not to impose sanctions for a violation of a rule, the ADA has no authority to recommend the sanction. (Van Andel, Tr. 1838–39) If Amway does impose a sanction, the distributor may bring the matter before the ADA Board. (Finding 80) Amway has bound itself by the decision of the Board on these arbitration cases. (Halliday, Tr. 6180)

Group boycotts are *per se* unlawful. In *Fashion Originators' Guild* v. *FTC,* 312 U.S. 457 (1941), a group of "original designers" agreed to refuse to sell their creations to retailers who had been selling copies of original designs. [83] The purpose of the agreement was to prevent style piracy, and the Court held that it was an unlawful group boycott and upheld the Commission's refusal to hear evidence on the reasonableness of the methods pursued by the combination. The issue involving the ADA, then, is whether the self-regulation is an unlawful group boycott like the *Fashion Originators'* case or whether it is pro-competitive.

Self-regulation by an industry has been allowed by the courts where:

(1) There is a legislative mandate for self-regulation. *Gordon* v. *New York Stock Exchange,* 422 U.S. 659 (1975).

(2) The collective action

(a) is intended to accomplish an end consistent with the policy justifying self-regulation
(b) is reasonably related to that goal, and
(c) is no more extensive than necessary.

enver Rockets v. *All-Pro Management, Inc.,* 325 F. Supp. 1049, 1064 .D. Cal. 1971).

The association provides procedural safeguards which assure that restraints are not arbitrary and which furnish a basis for judicial iew. *McCreery Angus Farms* v. *American Angus Ass'n.* 379 F. p. 1008, 1018 (S.D. Ill. 1974), *aff'd,* 506 F.2d 1404 (7th Cir.); *'ani* v. *NYSE,* 348 F. Supp. 1185 (S.D.N.Y. 1972).

The main purpose of the self-regulation by the respondents meets this test. (Findings 22, 78 and 80) [84]

"In an industry which necessarily requires some interdependence and cooperation, the *per se* rule should not be applied indiscriminately." *Hatley* v. *American Quarter Horse Ass'n,* 552 F.2d 646, 652 (5th Cir. 1977). In the direct selling of soap and detergents, "a few rules are essential to survivial." (*Ibid.*) Participation by the ADA as an arbitration panel does not by itself, without consideration of the specific rules involved, amount to a naked restraint of trade. An analysis of each rule alleged to violate the law is necessary to understand fully whether it is anticompetitive.

Discontinuance and Remote Evidence

Respondents argue generally that a substantial number of the exhibits relied on by complaint counsel are dated six years or more before the issuance of the complaint, and specifically that the customer protection rule, alleged to be evidence of retail price fixing, was dropped by Amway at the beginning of 1972.

Respondents rely primarily on *New Standard Pub. Co.* v. *FTC,* 194 F.2d 181 (4th Cir. 1952). In that case, the Commission issued an order six years after the last evidence was taken and the circuit court reversed and remanded. The court did not hold that the case was moot, but sent it back for more recent evidence. Respondents also rely on *Oregon-Washington Plywood Co.* v. *FTC,* 194 F.2d 48 (9th Cir. 1952). That case involved two groups which allegedly conspired to commit trade restraints. The respondents admitted the restraints had occurred up until seven years before the complaint issued and denied any further violation after that time. Complaint counsel did not put on any evidence, and the Commission issued an order based on the pleadings, relying upon a rule that a conspiracy once shown to exist is presumed to continue until abandonment is shown. The circuit court reversed, holding that the answers to the complaint denying the conspiracy put the matter in issue [85] and since complaint counsel did not put on any evidence and there was no such presumption, the complaint should have been dismissed. The court also held that there was nothing to show that the discontinued practices would be resumed and that discontinued practices do no provide a basis for an order.

The two issues here involve (1) the alleged discontinuance as defense, and (2) the age of the evidence.

The case law is clear that discontinuance of an illegal practice do not of itself render inappropriate the entry of a cease and des order. *Oregon-Washington Plywood Co.* v. *FTC,* 194 F.2d at 50–

The propriety of such an order in any particular case must depend on a consideration of all the surrounding facts and circumstances; and where the activities charged have been discontinued, the elements of time, volition and general attitude of the respondents in respect of the cessation are necessarily factors of prime importance. Parties who have abandoned their challenged practices only after proceedings are brought against them are in no position to complain of a cease and desist order. In such a case the discontinuance can hardly be thought voluntary.

And the cases have clearly held that discontinuance after the investigation has begun will not be held voluntary. *Giant Food, Inc.* v. *FTC,* 322 F.2d 977, 986–87 (D.C. Cir. 1963); *Cotherman* v. *FTC,* 417 F.2d 587, 594–95 (5th Cir. 1969); *Coro, Inc.* v. *FTC,* 338 F.2d 149, 153 (1st Cir. 1964), *cert. denied,* 380 U.S. 954 (1965). Here, Amway officially discontinued the customer protection rule in 1972 (although Amway has continued to urge distributors that such competition is "unethical"). (Findings 90–93) [86] Mr. DeVos told Direct Distributors in Dallas in 1971 the reason that the customer protection rule was goind to have to go (DeVos, CX 1037–E):

And I must be very frank with you—I think that the rule will have to go and it'll have to go probably in the not too far distant future. And the reason it'll have to go is that I don't think we can live with it any longer, I don't think we are consistent in our philosophy and I don't think the governmental people are gonna look at it favorably. They've already looked at it and they say that's a restraint of trade type thing, you see.[10]

The record shows that Amway knew of the Federal Trade Commission investigation in this case before January of 1970. (CX 345–E) The discontinuance of the customer protection rule by Amway was not the kind of abandonment of an illegal practice which gives assurance that it will not be repeated in the future. *Holiday Magic, Inc.,* 84 F.T.C. 748, 1050 (1974).

Some of the evidence relating to price fixing and customer restraints in this case goes back to the 1960's. Such evidence is relevant to show a continuing effort to fix prices and restrain competition. See *FTC* v. *Cement Institute,* 333 U.S. 683, 703–05 (1948), where the Court held that the Commission had properly regarded evidence as far back as 1902 in the price fixing case. And in *P.F. Collier & Son Corp.* v. *FTC,* 427 F.2d 261, 275 (6th Cir. 1970) the respondent had argued that the evidence was cold and stale, but the court upheld the Commission's order, stating that the fact that the evidence may be old does not mean that an order issued upon it is ...ted. The court held that where an illegal trade practice is ...ble of being perpetuated or resumed, it may be presumed to

...opping a practice after a visit by government investigators does not show permanent abandonment. *United ... Parke, Davis & Co.,* 362 U.S. 29, 47–48 (1960).

have been continued, [87] and an order may issue to prevent it, even upon a showing that it has been discontinued or abandoned.[11] Here, Amway had an explicit policy of retail price fixing in the middle 1960's, and, until 1972, a written policy of preventing distributors from competing with each other. This evidence raised a presumption that these policies have continued or could be resumed.

Count I—Price Fixing

The Rules of Conduct of the Amway Sales Plan published in 1963 required that distributors sell Amway products to consumers at the specified resale price. (Finding 109) It also provided that no unauthorized discount be given on sales to other distributors, and fixed the resale charge for freight. (Finding 109-111) The record does not show when Amway stopped using this sales manual or whether distributors were ever clearly notified that it does not express Amway's policy.[12] Such resale price maintenance is *per se* unlawful. *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.,* 220 U.S. 373 (1911). [88]

The Career Manual for Amway distributors published in 1968 specified that distributors should not cut the retail price in fund-raising drives. The fund-raising drive policy was changed in 1969, upon the recommendation of the ADA, so that the retail sales now are made by the distributor rather than by the fund-raising organization. (Finding 112) By implication at least, this change was made with the intent to control resale prices. While the policy requiring the distributor rather than the fund-raising organization to make the retail sales might be reasonable in itself, when coupled with unlawful intent it became an unreasonable restraint of trade. *United States* v. *Columbia Steel Co.,* 334 U.S. 495, 522 (1948).

While much of the evidence of price fixing agreements is relatively old, it raises a presumption of continuity which respondents have not rebutted.[13] After express contracts were no longer used, the other vertical restraints on advertising, selection of customers and sourc of supply controlled price competition. The customer protection ru alone stopped all competition for a retail customer for 30 days after distributor made a sale to that customer. (Finding 90) The purpose

[11] The court in *P.F. Collier* specifically declined to follow *Bearings, Inc.*, 64 F.T.C. 373 (1964), relied ‹ respondents. 427 F.2d at 275 n.13.

[12] On retail sales, Amway's price lists obliquely refer to "suggested retail for sales tax" or "retail sal computation base." (Finding 113) The record does not show that Amway has ever clearly told its distributo they are free to set their own prices on sales to other distributors or to consumers.

[13] *Holiday Magic, Inc.*, 84 F.T.C. 748, 1050 (1974). Amway was able to produce distributors who do us competitively to obtain wholesale and retail sales. (RPF 223-229) Considering the number of distributors Amway products, this is not surprising. Furthermore, evidence of price competition conflicts with state Amway officers who say that very little price cutting occurs. (Finding 127)

the customer protection role was "to prevent cut throat competition" between distributors. (Halliday, CX 486)[14] [89] Amway officially discontinued the rule only after Federal Trade Commission investigators looked at it and said it was a restraint of trade. (DeVos, CX 1037-E) Amway continues to support the principle of the customer protection rule by calling such competition "unethical." (Finding 93) One of the distributors testified to the effect of the customer protection rule in her organization. Mrs. Joan Spradley was asked by some of the distributors in her group if they could discount retail prices. She said "no." Mrs. Spradley testified that (Tr. 1340):

> It was our understanding that the retail price was a set thing, and that we did not compete with one another for customers. In other words, we understood when a Amway distributor made a contact, for instance, if I came to you and sold you Amway products, then you became my customer and under our ethics, another Amway distributor would not go and try to sell to you or undercut my price or anything like that. I would sell to you at the retail price and they would leave you alone and go get their own customers.

The customer protection rule has been used to support and continue the unlawful price fixing found herein and must be prohibited. "A practice which lessens price competition touches the core of the free enterprise system." *The Coca-Cola Company, et al.,* FTC Dkt. 8855 (Final Order dated April 7, 1978), at p. 89.

Amway threatens to terminate the distributorship of distributors who cut the retail price of Amway products. (Findings, 115, 117, 119) And where the price cutting distributor is not buying directly from Amway, the threat is made in combination with Direct Distributors. (Findings 115-117) Amway also encourages Direct Distributors to do a "sales job" on price cutting distributors, pointing out the reck-'essness of this conduct (Finding 115), and Amway urges that this hould be done through a combination of Direct Distributors. 'inding 116) [90]

Amway distributors promote the policy of discouraging price tting through their combined efforts with Amway. Price cutters ; quickly reproached by other distributors, and it is not long until ıway applies pressure directly and through Direct Distributors to) the "disturbance in the field." (Findings 117, 121) Many Amway ·ibutors are inexperienced in business (Van Andel, Tr. 1814-15) it does not take much pressure to stop price cutting. They :ly comply with the demands of Amway and other distributors ıp cutting retail prices. (Finding 117) *Holiday Magic, Inc.,* 84 748, 1049 (1974). While only a few distributors were actually

\mway market study in 1970 warned that lifting the customer protection rule could lead to "excessive g" by distributors. (CX 522-Z-215) coerced on this record (Findings 117, 121), price fixing agreements are unlawful *per se* regardless of enforcement. *Holiday Magic, Inc.*, 84 F.T.C. 748, 1049 (1974). And where the unlawful intent to fix prices is coupled with a single instance of coercion, even the Sherman Act will be violated. *Newberry* v. *Washington Post Co.*, 438 F. Supp. 470, 480-82, 485 (D.D.C. 1977). Here, the action by Amway in combination with Direct Distributors and other distributors to achieve uniform prices for Amway products would probably violate the Sherman Act, *United States* v. *Parke, Davis & Co.*, 362 U.S. 29, 45-46 (1960), and clearly violates Section 5 of the Federal Trade Commission Act which was intended by Congress to stop such conduct before it amounts to "full blown" violations of the Sherman Act. *FTC* v. *Brown Shoe Co.*, 384 U.S. 316, 320-22 (1966)

Amway quickly admonishes distributors who advertise Amway products at discount prices. (Findings 117, 119, 121) For example, Roger Laverty, an Amway distributor from Pompano Beach, Florida, had prepared sales literature using the Amway trademark, featuring price comparisons on Amway and competing products. An Amway Administrative Legal Assistant wrote to Laverty stating Amway's view of the law (CX 989-B): "[C]ost comparisons themselves are now strictly 'taboo,' are not used by Amway and should not be used by Amway distributors." On the contrary, however, the law protects price competition by truthful advertising. See *Sunbeam Corp.* v. *Payless Drug Stores*, 113 F. Supp. 31, 44 (N.D. Cal. 1953), citing *Prestonettes, Inc.* v. *Coty*, 264 U.S., 359, 368 (1924) (Mr. Justice Holmes): **[91]**

> A trade mark only gives the right to prohibit the use of it so far as to protect the owner's good will against the sale of another's product as his.... When the mark is used in a way that does not deceive the public we see no such sanctity in the word as to prevent its being used to tell the truth. It is not taboo.

Amway completes its control of retail prices by extending the bu back rule beyond its legitimate purpose—to prevent invento loading. Amway urges its distributors not to allow freight damag Amway products to reach the hands of salvage stores or if they dc buy them up before consumers can get to them. (Findings 122, 1

According to the Amway Career Manual published in 1968, Board of Directors of the association "meets at least three tir year to act on approval of product classifications for distrib under the Amway name, sales policies, pricing policies, discoun refund schedules . . . ." (CX 59-J) The record does not shov this policy has been discontinued. In fact, the ADA has cor with Amway in setting retail prices and has recommended changes and agreed with Amway on retail pricing policy. (Findings 79, 112(b))

Generally, a manufacturer who sells through independent wholesalers and retailers would prefer the lowest retail price possible, since that usually means increased sales and higher manufacturer revenues. *Continental T. V., Inc.* v. *GTC Sylvania, Inc.*, 433 U.S. 36, 56 n.24 (1977). Here, however, Amway's self-interest in preventing price cutting was indicated by Mr. Van Andel who reported in 1970 that a market test of Amway catalog products proved that the same products sold for a higher price led to 50% more sales, since the direct selling [92] distributors worked harder to obtain the higher margin. (CX 638-H) Since the higher price encourages distributors to do more selling, Amway does not sponsor special sales by granting extra discounts, and Amway sets the retail price of its catalog goods "competitive with the average department store level—without the specials." (*Ibid.*)[15]

The number of reports of distributors cutting the retail price of Amway products usually is something less than a dozen. (Halliday, CX 1040-H; DeVos, CX 1037-D). The "methods" employed by Amway and its distributors are "as effective as agreements in producing the result that 'all who would deal in the company's products are constrained to sell at the suggested prices.' " *United States* v. *Parke, Davis & Co.*, 362 U.S. 29, 42 (1960) (quoting *FTC* v. *Beech-Nut Packing Co.*, 257 U.S. 441, 455 (1922).

Empirical studies show that resale price maintenance does raise etail prices above what they would otherwise be. *Hearings on S.408 efore the Subcommittee on Antitrust and Monopoly of the Senate udiciary Committee*, 94th Cong., 1st Sess., p. 174 (1975). Such evidence l Congress to repeal the Miller-Tydings and McGuire Acts, which mitted states to enact "fair trade" laws authorizing sellers to ablish resale prices for branded commodities. 15 U.S.C. 1, 45 ective March 11, 1976). "Price is the 'central nervous [93] system of economy.' " *Nat'l. Soc. of Prof. Engineers* v. *United States*, 435 U.S. 1978-1 Trade Cases ¶61,990 at 74,225 (decided April 25, 1978). ondents regularly treat the subject of resale prices, however, in a er and informal manner.[16] "Price is too critical, too sensitive a

968, an Amway employee reported that retail prices on Amway products "are in most instances higher than comparable items in conventional retail outlets." (CX 558-B) Customer complaints about t prices (CX 700-J) may have changed Amway's pricing policy. In 1970, retail prices set for most og products were set below the prices for comparable items sold in department stores but above prices scount stores. (CX 522-Z-176 to 177)

Vos' advice to Direct Distributors on how to handle price cutting distributors exhibits a lack of nsistent with the sensitive nature of the subject. He incoherently mixes warnings of price fixings terminate the distributor or to badger, threaten and otherwise "do a sales job on the guy" because d against anything that's dog eat dog." (CX 1037-E to I) control to allow it to be used even in an informal manner to restrain competition." *United States* v. *Container Corp. of America*, 393 U.S. 333, 338 (1969). [94]

Counts II and III of the Complaint

Count II of the complaint alleges that respondents unlawfully allocate the Amway distributors' customers and source of supply. This allegation deals primarily with two rules of the Amway Sales and Marketing Plan: (1) the retail store rule requiring distributors not to allow Amway products to be sold through retail stores (Finding 85), and (2) the cross-group selling rule requiring distributors to sell Amway products only to distributors they have recruited and to buy Amway products only from their sponsor. (Finding 81)[17]

Count III of the complaint alleges that Amway restricts the advertising and promotional activities of the distributors. This allegation deals with the detailed regulation of its distributors' advertising. (Findings 94–108)

These rules are vertical in nature. Vertical customer allocations and requirements contracts are not the kind of "agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use." *Northern Pac. R. Co.* v. *United States,* 356 U.S. 1, 5 (1958). The vertical restrictions here must be analyzed under the rule of reason. *Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, 537 F.2d 980 (9th Cir. 1976), *aff'd,* 433 U.S. 36 (1977). [95] The *Sylvania* case involved location restrictions imposed on dealers by a small manufacturer competing in an oligopolistic market. 537 F.2d at 1001. The Court held that some vertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain marketing efficiencies in the distribution of its products. Among these "redeeming virtues," the Court found that established manufacturers may us[e] them to induce retailers to provide services necessary to the efficie[nt] marketing of the products and that new manufacturers may u[se] them to induce competent and aggressive retailers to do the wo[rk] necessary to distribute products unknown to consumers. 433 U.S. p. 55. The Court overruled the vertical *per se* rule stated in *Uni[ted] States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365 (1967) and, while foreclosing the possibility that particular applications of ver[tical] restrictions might justify *per se* prohibitions, the Court clearly that departure from the rule of reason standard must be based

[17] The customer protection rule has been considered a part of the unlawful price fixing combination, 88–89.

demonstrable economic effect rather than—as in *Schwinn*—upon formalistic line drawing. 433 U.S. at 59. No such economic effect has been proved here and the restrictions should not be treated under the *per se* rule.

Complaint counsel argue that: "Restrictions such as these should not be individually analyzed, for they work their toll on competition collectively." (CRB, p. 37) Nothing in the record compels the conclusion, however, that the restrictive provisions were employed in combination in an effort to eliminate or restrain competition to the detriment of consumers. *Snap-On-Tools Corp.* v. *FTC,* 321 F.2d 825, 830 (7th Cir. 1963):

> Except for the fact that the provisions are all found in one document, there is no evidence, let alone substantial, to show that these provisions were designed to be, or were employed as a *unitary device* to foster practices violative of Section 5 of the Act. (Emphasis by court.)

[96] Each restraint therefore must be analyzed individually to determine whether the preponderence of the evidence shows the prohibited purpose or effect.

The Amway Sales and Marketing Plan has involved wholesale and retail price fixing. If other restrictive practices were "ancillary" to this price fixing, or "part of a scheme involving price fixing," the result would be a *per se* violation of law. *United States* v. *Arnold, Schwinn & Co.,* 388 U.S. 365, 373 (1967); *White Motor Co.* v. *United States,* 372 U.S. 253, 260 (1963).[18] Here, however, no such finding can be made on this record. Here, the price fixing is ancillary and incidental to the other vertical restraints, to which respondents have spent most of their efforts. The other vertical restraints should therefore be judged independently from the price fixing. *United States* v. *Sealy, Inc.,* 388 U.S. 350, 351–52 (1967); *United States* v. *Arnold, Schwinn & Co.,* 388 U.S. 365, 373 (1967); *White Motor Co.* v. *United States,* 372 U.S. 253, 260, 263 (1963). [97]

Applying the rule of reason standard to vertically imposed territorial restraints, the Commission in *The Coca-Cola Company, et* FTC Dkt. 8855 (Final Order dated April 7, 1978) [91 F.T.C. 517], d that the vertical restraints involving nonrefillable bottles were roader scope than reasonably necessary[19] to achieve marketing

ı those cases, price fixing allegations in the complaints "accompanied" the allegations of other vertical ts, but the Court did not rely on that fact in deciding whether the *per se* rule should be used. The test is not price fixing allegations "accompany" allegations of other vertical restraints but whether the main ınd effect of all of the vertical restraints show a justifiable business reason, or whether they are mainly t fixing prices for which there is no acceptable economic basis. *(Ibid.)* The Commission referred to, but did p, this issue in the letter explaining the acceptance of a consent order in *Performance Sailcraft Inc.*, File . 2922] (Commission action dated May 2, 1978) [91 F.T.C. 869].

e the courts have split on adopting this part of the ancillary restraints doctrine (see dissenting opinion ioner Clanton in *Cola-Cola, supra,* at pp. 11–12), it was relied on in part of *Schwinn*, not reversed by

(Continued)

efficiencies by inducing capital investment, local advertising and promotional and service activities by the supplier's customers; and that intrabrand competition would be likely to invigorate price competition. The restrictions as to sales of the soft drinks in refillable bottles were, however, held reasonable because of practical marketing difficulties and consumer benefits associated with that product.

On this record, Amway's cross-group and retail store rules and its regulation of advertising, are reasonable and have provided entry to a marketplace[20] which would not otherwise have been available. (Dunlap, Tr. 6676–77) While this defense may not be a "perpetual license to operate in restraint of trade," *Siegel* v. *Chicken Delight, Inc.,* 448 F.2d 43, 51 (9th Cir. 1971), respondents' control of the distributors' marketing practices is no broader than necessary to achieve the main purpose of direct selling in an oligopolistic market.[21] [98] Furthermore, the restrictions here are not an "industrywide practice"[22] involving a "dominant brand" by an "established giant in the industry." (*Coca-Cola Co., supra,* at pp. 35, 47 and 51)

The Retail Store Rule

The Amway Sales and Marketing Plan requires that Amway products be sold directly to consumers and not through retail stores.[23] (Finding 85) Based upon evidence adduced through expert witnesses, Amway executives and numerous Amway distributors, it is apparent that the rule has preserved Amway's direct selling organization and consumer demand, and provided an incentive to distributors to furnish services to consumers.

Marketing experts gave credible testimony in this proceeding that if Amway products were sold in retail stores, distributors would lose interest in calling on consumers' homes, demonstrating and explaining products to create a demand which could be satisfied —perhaps at a lower price— at a retail store. (Finding 89) Without a demand for the products, retail stores would soon lose interest in Amway

Sylvania. The Court held that where Schwinn retained indicia of ownership it could, under the rule of reason, confine sales to franchised retailers for the reason, *inter alia,* that the restraint "was justified by, and *went no further* than required by, competitive pressures." 388 U.S. at 382. (Emphasis added.)

[20] While Amway sells a variety of products, its main business is still "selling soap." (RX 331, p. 4–A)

[21] Unlike some other direct selling companies, Amway does not prohibit distributors from selling competing products. (RX 331, p. 15–B; Bortnem - W.T. Raleigh, Tr. 697–99; Cooke - Avon Lady, Tr. 735–36; Laverty - Fuller Brush, W.T. Raleigh, Tr. 838–39). And, unlike Avon, the largest direct selling company, Amway does not assign sales territories to its distributors. (Cooke - Avon, Tr. 735; Halliday, Tr. 6192–93)

[22] Direct selling companies generally do not, however, sell their products through retail stores. (Patty, Tr. 3099–3103)

[23] Amway also prohibits distributors from selling or displaying Amway merchandise at flea markets and similar events (Finding 86) and regulates their sales through fund-raising drives. (Finding 87). The rationale for these restrictions is the same as the retail store rule and they have the same economic impact as that rule.

products. Amway would then be faced with the necessity of creating demand in the traditional way of advertising expenditures and **[99]** otherwise doing battle in the retail grocery stores, in a hostile oligopolistic marketplace. (Findings 171–181) Vertical restrictions on intrabrand competition may be used to allow a company to compete in an oligopolistic market. *Sylvania, supra.*[24]

The retail store rule gives Amway distributors an incentive to provide services to consumers and to create a consumer demand which would dissipate if Amway products were sold in retail stores. Amway distributors demonstrate and explain Amway products and deliver to the consumer's home. These services are typically unavailable from retail stores. (Finding 88) Because some Amway products are more concentrated than products sold in retail stores, demonstration and explanation are essential to consumer demand. (Diassi, Tr. 5529; Schroeder, Tr. 5355–56)

Vertical restraints which induce retailers to engage in promotional activities and to provide services help stir interbrand competition and should be encouraged. *Sylvania, supra; Snap-On Tools, supra,* 321 F.2d at 828–29. The retail store rule is such a vertical restraint and is lawful under the rule of reason. **[100]**

Cross-Group Selling Rule

The cross-group selling rule requires Amway distributors to buy Amway products only through their sponsor. (Finding 81) The distributors, in effect, promise to buy their "requirements" of Amway products from one supplier. There has been no showing on this record of any probable immediate or future market pre-emption which might substantially lessen competition. *Tampa Electric Co.* v. *Nashville Coal Co.,* 365 U.S. 320, 329 (1961).

The cross-group selling rule also provides that distributors shall sell at wholesale only to their sponsored distributors. This aspect of the rule has the same economic justification as the retail store rule.[25]

The cross-group selling rule is the basis for the Amway Sales and Marketing Plan. It provides the structure by which products, information and compensation flow from Amway to the Direct Distributors and down to the distributors engaged in making the retail sale. It provides lines of communication and responsibility insuring that distributors are properly trained and motivated and that consumers receive services provided under the Amway system

[24] Sylvania's market share was 5%, 433 U.S. 46–47 n.12, almost triple Amway's 1.7% of the soap and detergents market. (RX 406, RX 407)

[25] Amway also restricts distributors from selling non-Amway products to Amway distributors they have not sponsored. (RX 331, p. 15–B) The business reason for this restriction is to prevent a "conflict of interest." (Van Andel, Tr. 1896) The record does not show the market impact, if any, of this provision.

of distribution. (Finding 82) Used in conjunction with the performance bonus system, the cross-group selling rule gives sponsoring distributors an incentive to recruit, train, motivate and supply other distributors in order to gain a reward based on the sponsored distributors' sales volume. If sponsored distributors could buy Amway products from someone other than their sponsor, that incentive would not exist. The cross-group selling rule thus provides an alternative to payment of a "headhunting" fee as an incentive for recruiting. (Patty, Tr. 3111-13) **[101]**

Amway's Market Concept

Amway's marketing image was summarized well by one of respondents' expert witnesses (Diassi, Tr. 5542-43):

> I would think that it is based a great deal on the form of the product, that is, it is a concentrated product for the consumer. It is one that she has to use very little of per washload and therefore economical to use. I think that they have built in one other feeling for it and that is the idea that it is delivered directly to the home. There is a service portion that is built into the, into that product itself.
>
> I think to a certain degree that there is some exclusivity built into it, too, that you can only buy it from an Amway distributor. It is not a product that everyone can get ahold of, although I am sure Amway would like to have everyone buy the product. But I think those are the ingredients that go into it. It is a very high quality sophisticated product that almost requires somebody to tell you how to use it as opposed to something that is in a supermarket that you just go out and kind of dump into the machine.

The concept of which market a company like Amway wants to compete in has been protected by the courts which have upheld rules, more restrictive than those involved here, because they were necessary to maintain that concept. In *Evans* v. *S.S. Kresge Co.,* 544 F.2d 1184 (3d Cir. 1976), *cert. denied,* 433 U.S. 908 (1977), a department store chain licensed the use of the K-Mart service trademark and a "one stop shopping" concept to various independent food stores. The resulting retail outlet was comprised of the independent food store and the chain department store under one roof with one K-Mart sign appearing outside. The department store chain was interested in drawing on customers making frequent food purchases **[102]** at the grocery stores. In order to retain its reputation and market concept for high volume and low prices, Kresge required the grocery stores, *inter alia,* to agree to set prices on their non-food items (2%-5% of their volume) at prices no higher than the prices charged by the department store for the same items. The Third Circuit Court of Appeals upheld the summary judgment for Kresge, holding that there was no violation of the Sherman Act (544 F.2d at 1193):

> . . .[T]he challenged restraint enabled Kresge to add a food component to its discount operation without causing customer confusion or threatening the low-price "K-Mart" discounting image upon which the success of K-Mart (including K-Mart Food) would depend. Therefore, far from attempting to stifle competition, the restraints had as their purpose the stimulation of business and efficiency for both the department store and the supermarket: they (the restraints) would assure that the overall operation would compete effectively in both the discount and food markets vis-a-vis other department store and food discounters. The restraints thus serve a legitimate business purpose.

The trademark licensor's market concept was also upheld in *Weight Watchers of the Rocky Mountain Region, Inc.* v. *Weight Watchers Int'l, Inc.*, 1976-2 Trade Cas. §61, 157 (E.D.N.Y. 1976). There, Weight Watchers International had licensed its trademarks and system of weight control to over 100 independent franchisees. The franchise agreement prohibited the franchise from offering "front loading" or "prepayment" plans whereby the members were asked to prepay their fees for weight control classes to be held in the future in return for which they received discounts and some meetings without charge. Weight Watchers International prohibited prepayment plans because other weight loss clubs had engaged in fraudulent practices in connection with such arrangements. The plaintiff franchisee [103] nevertheless required prepayment, arguing that it put pressure on members to attend weight classes. Weight Watchers International argued that its marketing concept was that no commitment by the member was central to its weight plan. The court held that the rule was consistent with the antitrust laws and that the franchisee had interfered with the defendant's central marketing concept (at p. 70, 226): "[Weight Watchers International's] limitation on price policy is . . . an integral part of its method. Any modification of it might do serious damage to the good will of International."

The market concept by which Amway has, in less than 20 years, successfully added a new competitive presence to the oligopolistic soap and detergents market, among others, depends on the vertical restraints imposed on the distributors such as the retail store rule and the cross-group selling rule. Any modification of these rules might well do serious damage to this marketing concept and Amway's goodwill.

Trademark and Servicemark Protection

Amway argues that it has established several rules, including the retail store rule and those regulating distributors' advertising, in order to protect its goodwill and trademarks and servicemarks.

The owner of a mark must prevent third parties from misusing a mark or will be deemed to have abandoned it. *Dawn Donut Co.* v. *Hart's Food Stores, Inc.*, 267 F.2d 358, 366 (2d Cir. 1959).[26] **[104]** This means that a trademark owner has the right to supervise to some extent the quality of goods and services offered by licensees under that mark. *Siegel* v. *Chicken Delight, Inc.*, 448 F.2d 43, 51 (9th Cir. 1971), *cert. denied*, 405 U.S. 43; *Denison Mattress Factory* v. *Spring-Air Co.*, 308 F.2d 403, 409 (5th Cir. 1962). It does not mean, however, that merely because restrictive provisions are part of a trademark licensing arrangement those provisions are immunized from the antitrust laws, where their central purpose is to restrain trade. *Timkin Roller Bearing Co.* v. *United States*, 341 U.S. 593, 598–99 (1951). Specifically, a manufacturer cannot maintain resale prices under the theory that discount prices will interfere with trademark rights. *Sunbeam Corp.* v. *Payless Drug Stores*, 113 F. Supp. 31, 44 (N.D. Cal. 1953). Protection of the goodwill embodied in a trademark may, however, justify an otherwise invalid trade restraint such as a tying arrangement. *Susser* v. *Carvel Corp.*, 332 F.2d 505, 512 (2d Cir. 1964). And the worth of the trademark will be assessed in determining the reasonableness of requirements contracts, *Denison Mattress Factory* v. *Spring-Air Co., supra*, at p. 410, and customer limitations, *Perma Life Mufflers, Inc.* v. *International Parts Corp.*, 392 U.S. 134, 136 n.4 (1968).

It is apparent, therefore, that the protection of Amway's trademarks and servicemarks carry weight in the determination of the legality of the vertical restraints it has imposed on the distributors.

Amway meticulously regulates advertising by its distributors. (Findings 94–108) Except for Amway's control of price advertising, *supra*, this control of advertising has adequate legal support. Amway has an "affirmative duty to itself and to the public to invoke some kind of control and restraint" in order to guard against misuse of its marks. *Denison Mattress Factory* v. *Spring-Air Co., supra*, at p. 409. The trademark licensor may properly regulate advertising or promotional materials in connection with the licensing of trademarks. **[105]** *Weight Watchers of the Rocky Mountain Region, Inc.* v. *Weight Watchers Int'l, Inc.*, 1976-2 Trade Cas. ¶ 61,157, at p. 70,225 (E.D.N.Y. 1976). And Amway had the right to regulate its distributors' advertising to stop infringement of its marks by unauthorized

[26] The rights of servicemark owners in this respect are the same as owners of trademarks. *Pro. Golfers Ass'n* v. *Bankers Life & Cas. Co.*, 514 F.2d 665, 668 (5th Cir. 1975)

publication in sales literature. *Amway Corp.* v. *International Sales Aids, Inc.,* 187 U.S.P.Q. 15, 21–22 (E.D. Ark. 1974).

Complaint counsel raise as a collateral issue the validity of three servicemarks. (CRB, p. 64) They argue that Amway distributors do not in fact perform services not normally connected with the sale of a particular type of product, and that a servicemark should not have been issued. Amway distributors do, however, perform valuable services for their sponsored distributors. (Finding 82) And Amway distributors provide valuable services to consumers, demonstrating and explaining products and delivering the products to the customer's home or place of business. (Finding 88)

Complaint counsel further attack the validity of the servicemarks, alleging "something highly improper" (CRB, p. 71 footnote) in an affidavit filed in support of the application for the servicemark. Although complaint counsel do not cite the record in this regard, they apparently refer to an error made in the application which referred to "trademark" rather than "servicemark." (Price, Tr. 2881) The context of the entire application shows that it involves a request for protection for a trademark for services.

Complaint counsel also argue that the application filed in support of the mark stated that it was for "door-to-door retail merchandising engaged in by the distributors," whereas respondents have discouraged "door-to-door" selling. (CRB, p. 72) The term "door-to-door" selling has a generic sense meaning "direct selling" as opposed to selling to retail stores. Amway advises its distributors to try to get an introduction from a neighbor, customer or friend before knocking on someone's door, although door-to-door canvassing is used by Amway distributors and it is "optional with them." (Van Andel, Tr. 1757–58) **[106]**

Counts IV and V of the Complaint

Counts IV and V of the complaint allege that respondents' system of distribution is unfair and involves misrepresentations concerning the nature of the system and the income distributors may gain from recruiting and fails to disclose distributors' substantial expenses and turnover.

Pyramid

Complaint counsel argue that the Amway Sales and Marketing Plan is inherently unlawful because it is "a scheme to pyramid distributors upon ever increasing numbers of other distributors." They argue that the Amway Plan, even without actual proof of economic failure, is "doomed to failure" and contains an "intolerable potential to deceive." (CB, p. 32)

This rule of *per se* illegality for pyramid plans has not yet been accepted by the courts. *Ger-Ro-Mar, Inc.*, 84 F.T.C. 95 (1974), *rev'd in part, Ger-Ro-Mar, Inc.* v. *FTC*, 518 F.2d 33, 37 (2d Cir. 1975); *United States* v. *Bestline Products Corp.*, 412 F. Supp. 754, 777 (N.D. Cal. 1976). The Commission defined such unlawful "entrepreneurial chains" in *Koscot Interplanetary, Inc.*, 86 F.T.C. 1106, 1180 (1975):

> Such schemes are characterized by the payment by participants of money to the company in return for which they receive (1) the right to sell the product *and* (2) the right to receive in return for recruiting other participants into the program rewards which are unrelated to sale of the product to ultimate users. In general such recruitment is facilitated by promising all participants the same "lucrative" rights to recruit. (Emphasis in original.)

[107] Participants in the Koscot marketing plan paid an initial amount up to $5,000 to the company for inventory and the right to recruit others. The distributors who recruited others received $2,650 of the recruit's $5,000 payment. 86 F.T.C. at 1179. The only way a Koscot distributor could get the payment back was to recruit more distributors. 86 F.T.C. at 1131. Koscot and its distributors were primarily in the business of selling distributorships. 86 F.T.C. at 1140.

Participants in the *Ger-Ro-Mar, Inc.* marketing plan bought non-returnable inventory for up to $1,950. 84 F.T.C. at 108–10. Recruiters received compensation based on the fact of recruiting regardless of whether products were sold to the consumers. 84 F.T.C. at 148.

The pyramid marketing program in *Holiday Magic, Inc.*, 84 F.T.C. 748 (1974) required distributors to buy in at various levels for up to $4,500. At the highest level, distributors received $2,500 of the $4,500 for recruiting another distributor at the same level. 84 F.T.C. at 1032. The inventory purchased in this manner was non-returnable and the company paid little attention to consumers. 84 F.T.C. at 1035.

There is little doubt that a pyramid distribution scheme should now be condemned even without the demonstration of its economic consequences. The Commission has studied the effects of such "entrepreneurial chains" and seen the damage they do and a *per se* rule should be used. *Koscot Interplanetary, Inc.*, 86 F.T.C. 1106, 1180–82 (1975). Such a rule would be based on demonstrated economic effect in these cases, rather than formalistic line drawing. *Continental T.V. Inc.* v. *GTE Sylvania Inc.*, 433 U.S. 36, 59 (1977). In such cases, the fact that some retail sales occur does not mitigate the unlawful nature of the method of recruiting. *Ger-Ro-Mar, Inc.*, 84 F.T.C. 95, 148–49 (1974), *rev'd on other grounds*, 518 F.2d 33 (2d Cir.

1975). Here, however, the Amway system does not involve an "investment" in inventory by a new distributor. (Finding 61) A kit of sales literature costing only $15.60 is the only requisite. (Finding 34) And that amount will be returned if the distributor decides to leave Amway. (Finding 37) [**108**]

The Amway system is based on retail sales to consumers. (Findings 72–75, 144) Respondents have avoided the abuses of pyramid schemes by (1) not having a "headhunting" fee; (2) making product sales a precondition to receiving the performance bonus; (3) buying back excessive inventory; and (4) requiring that products be sold to consumers. (Patty, Tr. 3092–94). Amway's buy-back, 70% and ten customer rules deter unlawful inventory loading. (Findings 145–47)[27] Amway is not in business to sell distributorships and is not a pyramid distriubtion scheme. (Findings 142–44)

Saturation

The complaint alleges that distributors are not long likely to recruit other distributors because "recruitment of additional participants must of necessity ultimately collapse when the number of persons theretofore recruited has so saturated the area with distributors or dealers as to render it virtually impossible to recruit others." (Complaint, p. 9)

The term "saturation" as used in the complaint and by complaint counsel is one of the legitimate proofs in a case involving a pyramid distribution scheme. *Koscot,* 86 F.T.C. at 1135; *Holiday Magic,* 84 F.T.C. at 979; *Ger-Ro-Mar,* 84 F.T.C. at 119. Since Amway is not such a pyramid, the concept is immaterial here. [**109**]

Irrespective of the materiality of the concept, the facts in this record do not show that Amway distributors in any market were unable to recruit new distributors or to sell Amway products because of any inherent defect in the Amway Sales and Marketing Plan.[28] Products are consumed or wear out. (Patty, Tr. 3110) The population of the country continues to grow and to move about. Only one in four Amway distributors engage in recruiting, and there has been no decline in that percentage in recent years. The sales trend for Amway has shown almost uninterrupted growth. (Finding 151) The markets for Amway products and distributors, in short, are not static.

The preponderence of the evidence in the record does not support

[27] While the ten customer rule has a reasonable basis in preventing an unlawful pyramid, the distributors' monthly reports showing such sales need not specify the prices at which the sales were made. Such a requirement could be used to monitor unlawful resale price fixing.

[28] According to a market study conducted in 1973, only 4% of the distributors who did not renew their distributorship left because there were too many other Amway distributors in their area. (CX 521-E)

the allegation of "saturation." (Findings 148–52) From my observation of the demeanor, inconsistencies and uncertainties in the testimony of the witnesses called in support of the complaint in this regard, I believe the reason for their failure was more accurately described by a marketing expert who testified about this subject (Patty, Tr. 3109): "I think generally speaking when a salesman tells you that a market is saturated, he has become discouraged for some reason, usually he is simply not making the sales effort that is required." [110]

Misrepresentations and Failure to Disclose

The complaint alleges that respondents falsely represent that it is easy to recruit distributors and that distributors will receive substantial earnings. The complaint also alleges that respondents fail to disclose that there is substantial turnover among Amway distributors, and that substantial expenses are incurred in the business of being an Amway distributor. (Complaint, pp. 13–14) Misrepresenting to potential salespersons the nature of the position offered and the amount of compensation that will be received violates the Federal Trade Commission Act. *Encyclopedia Britannica, Inc.,* 87 F.T.C. 421, 488 (Initial Decision adopted by the Commission 1976).

Misrepresentations

The complaint alleges that respondents unlawfully represent that sponsoring is easy and profitable. (Complaint, pp. 10, 13) While words such as "easy" and "profitable" are relative, they can be the basis for a proper charge of unlawful misrepresentation. *Tashof* v. *FTC,* 437 F.2d 707, 712 (D.C. Cir. 1970); *Goodman* v. *FTC,* 244 F.2d 584, 597 (9th Cir. 1957); *Steelco Stainless Steel, Inc.* v. *FTC,* 187 F.2d 693, 697 (7th Cir. 1951); *contra, Carlay Co.* v. *FTC,* 153 F.2d 493, 496 (7th Cir. 1946). The facts, however, show that no unlawful misrepresentation has occurred.

Amway has represented that: "Sponsoring is easy!" Such isolated statements are found in detailed literature about the Amway Sales and Marketing Plan which must be read in context in assessing the nature of the statement. (Finding 139) Furthermore, Amway lets distributors know that the Amway Sales and Marketing Plan involves work. (Finding 130) In the introduction to the Career Manual for Amway Distributors, Mr. DeVos tells new distributors [111] that they are getting into the business on the "ground floor," starting "at the bottom," and that the Amway plan is an opportunity for all "who are willing to pay the price for success" and that the "person who thinks he can get big without working has no place here." (RX 331, p. 3-A)

In support of the allegation complaint counsel have proposed only the finding that three out of four distributors do not recruit. (CPF 525) This has little to do with the ease of recruiting because there has been no showing that all distributors are interested in recruiting rather than retail selling. Moreover, complaint counsel seem to admit that Amway has had no trouble recruiting distributors. (CB, p. 10).[29]

There is no doubt that the Amway Sales and Marketing Plan is designed to catch the interest of a prospective recruit by appealing to material interests. (Findings 59, 138) One approach is the "dream" sheet. Prospects are asked to describe their goals and dreams such as "a new car, a new home, college education for your children." They are, however, also asked: "Are you willing to work hard to get this?" (Finding 59)[30] [112]

Amway literature and speeches made at rallies by Amway representatives describe luxuries that may be available to Amway distributors. (DeVos, CX 1000-Z-3; Findings 59, 131) Guides for presenting the sales and marketing plan instruct the distributor to tell prospects (CX 190-J):

> For *you* the Amway Sales and Marketing Plan can mean the kind of life you've always dreamed of living, a new car, a new home, security . . . the things you want most out of life can be yours! Amway can be the means by which you achieve those things you've always dreamed of, but never thought you could afford. Amway can offer you an opportunity for true independence. Freedom from time clocks and freedom to travel *when* you want to. . . . [F]reedom from allowing someone else to decide your financial progress. (Emphasis in original.)

But the Amway plan also makes clear the idea that work will be involved, and that the material rewards to be gained will directly depend on the amount and quality of work done. (Finding 130) Complaint counsel argue that appealing to financial and material goals of salespersons is "emotionally exploitative." No applicable

[29] They argue that Amway has too many distributors and that Amway has "saturated" the market for distributors.

[30] Complaint counsel object to the "curiosity approach" that distributors have used when attempting to interest recruits. This involves getting the prospect to attend a meeting by a statement such as "we're in the business of helping professional people . . . start their own business," without mentioning the name "Amway." (Williams, CX 1116-S - T) At the meeting the full details of the Amway Sales and Marketing Plan are then explained. This approach was used primarily in the early 1970's because of the adverse publicity about pyramid plans unconnected with Amway. (CX 519-Z-49)

Amway distributors are not required to seek new distributors only by first announcing to prospects that they want to take their leisure hours away in a sales job. One distributor said that if this approach is used and ". . . you're talking to the guy that just came home from a factory maybe after ten hours, and is perspiring and looking at you and saying, 'Lady, you are one big dingaling if you think I'm gonna go out and do some more work after that.' " (Blinco, CX 1041-Z-3) precendent was cited or found that would hold such conduct unfair. [113]

Amway literature urges recruiters not to "quote dollar incomes on specific individuals even though you may want to use their stories about the homes in which they live, the cars they drive, or the airplanes they fly." (Finding 131)[31] Amway officers and other representatives have, however, orally stated specific dollar incomes which are attributed to Amway distributors. (Finding 132) These statements are typically made in mass sales rallies which are primarily for persons who are already Amway distributors. (Finding 48; CX 57-Z-118) The context of the sales talk is inspirational and it is to a knowledgeable crowd already aware of the details of the Amway Sales and Marketing Plan,[32] and in this motivational context the statements are obviously meant and understood to be feasible goals and not guaranteed average income for the listeners.[33] [114]

Amway recommends that distributors explain the Sales and Marketing Plan by using specific dollar amounts representing hypothetical retail and wholesale sales. (Findings 60, 134, 135) This method explains visually how to receive income by recruiting new distributors. It is frequently referred to as "drawing the circles" (CX 116-I) and shows expanding organizations of distributors in four or five examples, culminating in a hypothetical organization showing the sponsoring distributor receiving hundreds of dollars in monthly gross income. The diagrams start with a specific amount for the sponsoring distributor's hypothetical retail sales. From 1973 until 1977 this amount was $200 B.V.[34] Until recently Amway's circle diagrams showed the sponsored distributors' hypothetical sales also as $200 B.V. In 1977 recruiting literature, Amway changed these to more realistic varying amounts. (RX 401, pp. 7-9)

The circle diagrams have been qualified in the Amway literature to show that the illustration is hypothetical. (CX 162-G):

> For example, let's say you begin by sponsoring six new distributors. Just to illustrate the way the Amway Sales Plan operates, and not to suggest that there is any predictable level that any individual will ordinarily achieve, let us assume that each of the six sells an order a day . . . $5 a day . . . $100 per month . . . though actual sales will vary. . . .

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[31] Specific examples of amounts paid to Amway distributors are well qualified in the literature to show that they are maximum amounts, not average. (RX 401, p. 10)

[32] Amway urges that recruiting be done individually rather than at mass meetings. (CX 638-H)

[33] For example, while urging distributors to open their minds to thinking in terms of making $100,000 a year, Mr. DeVos predicted that "there are going to be *some people* in the room" who were going to have that kind of income. (Finding 132) (Emphasis added.) This statement does not indicate that the average distributor can expect to make that amount. Examples cited in complaint counsel's proposed findings, when put in context, similarly show that the speakers are offering the specific amounts as goals not as representations of average incomes. (See the text surrounding the dollar amounts referred to in CPF 457, for example CX 990-Z, CX 992-H, CX 992-J.)

[34] Before 1973 it was $100; in 1977 it was raised to $250. (Finding 134; RX 401, pp. 7-9).

NOTE: Volume figures and earnings shown in this session are meant for *example* only. In actuality, distributors may show a variety of different volumes and earnings. Growth of an Amway group is not likely to work out in just this way.[35] (Emphasis in original.)

[115] The average Amway distributor sells far less than $200 a month. (Finding 137) The vast majority of Amway distributors are in the business part-time. Only one in four sponsors other distributors, and many apparently are distributors in order to buy Amway products—at about a 30% discount—which they consume. (Finding 137) For a dollar figure representing average sales by distributors engaged in active retailing of Amway products, however, the $200 is reasonable. (Cliett, Tr. 3759; Bryan, Tr. 4521)

Mr. Van Andel's reason for using the $200 figure is to act as a goal to motivate the distributors' sales. (Finding 136)[36] One of complaint counsel's [116] witnesses, Jack Wayne Hearne, a former Amway distributor, testified that he understood the $200 figure was a goal, not an average (Tr. 632–33):

Q. I believe you said that at the first meeting [the prospective distributors] were told that part of the plan was that everyone should try to sell $200 worth of products a month, that is correct?

A. Yes, and I asked why, and [the Amway distributor] said this is the basic thing that we work for. You are not required. If you do fine, if you don't fine, whatever. That was the goal you kind of worked toward.

The Amway literature stresses that retail selling is essential, and that sponsoring new distributors brings the responsibilities of training, motivating and supplying. The literature also warns the distributor never to give the imprssion that a business can be built only by sponsoring new distributors and not to quote dollar incomes by specific distributors or otherwise to imply that the plan is for anyone "who is unwilling to work hard." (RX 331, pp. 8–D, 9–D) In this context, it is clear that drawing the circles to show the Amway plan is not an attempt to deceive prospects into believing that such earnings are "typical" for Amway distributors, *Goodman* v. *FTC,* 244 F.2d 584, 595–96 (9th Cir. 1957), or that distributors "will obtain" the

[35] And distributors were warned: "In reality, some of your distributors will probably sell more than $200 P.V. while others may sell less; but just to make it easy to understand, we'll stick to the figure of $200 P.V. for purposes of this example." (CX 190–G; CX 201–G)

And Amway literature advises that: "As with retailing, depending on their own goals, initiative, and available time, and the retail sales of those they sponsor will vary." (CX 205–G; CX 208–F)

[36] The audience at opportunity meetings includes persons who are already distributors as well as prospective distributors. (CX 204–G) The "drawing circles" technique is used to teach these distributors the wholesale side of the Amway Sales and Marketing Plan and to set goals for these distributors, as well as to introduce prospective distributors to the plan.

amount specified. *Tractor Training Service* v. *FTC*, 227 F.2d 420, 425 (9th Cir. 1955), *affirming*, 50 F.T.C. 762, 769, 774.

For the same reason, there is no law violation in Amway's use of the $1000 figure as the earnings of a business which a distributor "may build." (Finding 138) There is no doubt that some Amway distributors earn that amount. (Finding 133) [117] It is used to entice prospects to an opportunity meeting where the details of the Amway Sales and Marketing Plan can be explained. In the context of the plan, it is clear that the amount is not meant to represent the average or typical earnings of an Amway distributor.[37]

Amway is not a "modern-day version of the chain letter." *Holiday Magic, Inc.*, 84 F.T.C. 748, 1035 (1974) The Amway system does not create the potential for massive deception present in a pyramid distribution scheme which relies primarily on the profits to be made from recruiting new distributors rather than from ultimate sales to consumers. (*Id.* at 1036) Unlike the pyramid companies, Amway and its distributors do not make money unless products are sold to consumers. The inherent potential for deception is not present in the Amway plan. In the full context of the plan, it does not have an unlawful capacity to deceive. [118]

Failure to Disclose

Respondents have not misrepresented the potential expenses incurred in running an Amway distributorship. Amway literature describes normal business expenses involved in conducting a distributorship, even assuming the distributors were not already aware of the existence of such expenses. (Finding 140)

The complaint also alleges that Amway has failed to disclose that there is a substantial turnover of persons recruited as Amway distributors.

Amway experienced a decline in the number of distributors recruited into its system starting about 1971. This lasted for a few years and was caused primarily by bad publicity concerning pyramid distribution companies. (CX 519–G, U) In recent years, the total number of Amway distributors has been increasing gradually and the rate of turnover has been falling. (Finding 148)

Direct selling companies typically have a high turnover among their independent salespersons. (Finding 162)[38] The rate of turnover

[37] In any event, prospective Amway distributors do not believe that they will make $1000 a month. On the application form for an Amway distributor, the applicants are asked to state their expected earnings. About 90% expect to earn less than $10,000 a year. About 75% expect less than $5,000, and more than half expect less than $2,000 a year. (CX 516–U)

[38] *Compare*, *Snap-On-Tools Corp.* v. *FTC*, 321 F.2d 825, 829 (7th Cir. 1963). Of 900 dealers of industrial tools, Snap-On had a turnover of from 350 to 700 in one and one-half years.

among Amway distributors has been lower than average among direct selling companies. (Findings 148, 162, 163) Furthermore, Amway warns its distributors that newly sponsored distributors can be expected to leave the business. (Finding 141) **[119]**

Conclusions

The Amway Sales and Marketing Plan is not a pyramid plan. In less than 20 years, the respondents have built a substantial manufacturing company and an efficient distribution system, which has brought new products into the market, notably into the highly oligopolistic soap and detergents market. Consumers are benefited by this new source of supply, and have responded by remarkable brand loyalty to Amway products. (Finding 186) The vertical restraints by which Amway has achieved this entry—avoiding conventional retailing through grocery stores by direct selling—are reasonable. Respondents' restraints on price competition, however, must be prohibited.

I therefore conclude that:

1. The Federal Trade Commission has jurisdiction over respondents and the subject matter of this proceeding.
2. This proceeding is in the public interest.
3. Respondents have agreed, combined and conspired with each other and Amway distributors to fix resale prices for Amway products, on sales between Amway distributors and to consumers, in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45.
4. The attached order to cease and desist against respondents is appropriate, supported by the findings of fact, reasonably related to the offenses found, and necessary for the protection of the public interest.
5. The record does not support the allegations of Counts II, III, IV and V. Accordingly, those counts must be dismissed. **[120]**

Remedy

The order in this case should prohibit respondents in the future from controlling the prices charged for Amway products in sales between distributors and to consumers. And since the customer protection rule had that purpose and effect, the order must cover allocation of retail consumers.

As long as they obey the other rules herein found to be reasonable, distributors should have the right to advertise and sell Amway products, which they have purchased, at whatever price they wish.[39] "[W]here consumers have the benefit of price advertising, retail prices often are dramatically lower than they would be without advertising." *Bates* v. *State of Arizona,* 433 U.S. 350, 1977–2 Trade Cases, ¶ 61,573, at p. 72,330. [121]

ORDER

I

It is ordered, That respondents Amway Corporation and Amway Distributors Association of the United States, their officers, agents, representatives, employees, successors and assigns, and respondents Jay Van Andel and Richard M. DeVos, individually, and their agents, representatives and employees, directly or indirectly, or through any corporate or other device, in connection with the offering for sale, sale or distribution of any product, whether by combination, agreement, conspiracy or coercion, shall forthwith cease and desist from:

1. Fixing the price at which any distributor may advertise, promote, offer for sale or sell any product at retail.
2. Fixing the price at which any distributor may sell any product to any other distributor.
3. Requesting or obtaining any assurance to comply with, continuing, enforcing, or announcing any contract, agreement, [122] understanding, or arrangement with any distributor or prospective distributor which fixes the price at which any product is sold or advertised by such distributor or prospective distributor.
4. Threatening to withhold or withholding bonus payments or profit sharing payments from any distributor because of the price at which said distributor advertises or sells any product.
5. Requiring or requesting distributors to report the price at which products are resold, or to report the identity of any other distributor because of the retail price at which such distributor is advertising or selling any product; or acting on any reports or information about such retail prices by threatening, intimidating, coercing, terminating or contacting in any way the said distributor because of those reports or information. [123]
6. Terminating or taking any other action to prevent or limit the sale of any product by any distributor because of the retail price at

[39] Mr. Price, Amway's trademark attorney, testified that distributors can properly advertise that they are selling Amway products. (Tr. 2900–01)

which the distributor is advertising or selling any product, whether or not in conjunction with any of the Amway trademarks or servicemarks.

7. Publishing or distributing, directly or indirectly any wholesale or retail price list, order form, promotional material or any other document which employs resale prices for products sold by respondents without stating clearly and conspicuously in conjunction therewith the following: "The prices stated herein are suggested prices only. Distributors are not obligated in any way to adhere to any suggested prices. Distributors may determine for themselves the prices at which their product may be sold to other distributors or to consumers."

8. Allocating retail customers of distributors. [124]

II

Nothing in this order shall affect:

1. Respondents' rights in law and equity respecting the protection of respondents' trademarks or servicemarks in conjunction with the offer for sale or advertising of any product.

2. Respondents' rights to enforce the rules of the Amway Sales and Marketing Plan found reasonable in this decision.

III

It is further ordered, That respondent Amway Corporation, or its officers, agents, representatives, employees, successors or assigns, shall:

1. Within thirty (30) days from the effective date of this order, deliver a copy of this order to cease and desist to all present Amway Direct Distributors and distributors. From each Direct Distributor, a signed statement acknowledging receipt of this order shall also be obtained. [125]

2. Deliver a copy of this order to all future Amway distributors on the date of their participation.

3. Within thirty (30) days of the effective date of this order, make written offers of distributorships of equivalent value to the distributorship of any distributor who was terminated or suspended solely for the violation of rules, or policies which contravene any of the provisions of this order.

IV

It is further ordered, That respondents and their successors and assigns notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondents such as dissolution, assignment or sale resulting in the emergence of successor corporations, the creation or dissolution of subsidiaries or any other change in the corporations or in the Amway Sales and Marketing Plan which may affect compliance obligations arising out of the order. [126]

V

It is further ordered, That the individual respondents promptly notify the Commission of any change of their present business relationship or employment. Such notice shall include respondents' business address and a statement as to the nature of change of business or employment as well as a description of their duties and responsibilities.

VI

It is further ordered, That the respondents herein shall within sixty (60) days from the effective date of this order, file with the Commission a report in writing setting forth in detail the manner and form in which they have complied with this order.

Opinion of the Commission

By Pitofsky, *Commissioner:*

I. Introduction

In March 1975 the Federal Trade Commission issued a complaint charging respondents Amway Corporation ("Amway"), Amway Distributors Association ("ADA"), Jay VanAndel (Chairman of the Board of Amway and one of its two principal owners), and Richard M. DeVos (President of Amway and the other principal owner), with various violations of Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45. The alleged violations involve the distribution network that has been built up to market the consumer products Amway manufactures. [2]

After extensive discovery, hearings began in May 1977 and were concluded in October 1977. In an Initial Decision rendered June 23, 1978, the presiding administrative law judge (the "ALJ") found that FTC counsel supporting the complaint ("complaint counsel") had established that respondents had engaged in illegal resale price maintenance, but had failed to establish that respondents had committed other violations of Section 5. We affirm the ALJ's decision with respect to resale price maintenance and, in addition, find that respondents have made false and misleading earnings claims in attempting to recruit persons to serve as distributors of Amway products. We also agree with the conclusion reached in the Initial Decision, that complaint counsel have failed to prove the other allegations made against Amway of unfair methods of competition and unfair or deceptive acts and practices. Specifically, we have determined that the Amway Sales and Marketing Plan is not an illegal "pyramid scheme"; that the non-price-related rules Amway has imposed on the distributors of its products, to control the way the products flow to consumers, do not constitute unreasonable restraints of trade or unfair methods of competition; and that, with the exception of certain earnings claims, respondents have not made false, misleading, or deceptive claims about Amway's business or the opportunities it presents to a person who becomes a part of it.

Amway has a highly unusual distribution system, and therefore a fairly extended description of Amway's business and marketing techniques is necessary as a prologue to the application of the relevant legal principles.

A. The Nature of Amway's Business

Amway was formed in 1959 by VanAndel and DeVos. It manufactures over 150 products, most of which are cleaning and personal care products. Soaps and detergents constitute 41 percent of sales; polishes, sanitation goods, and other cleaners 20 percent; toilet preparations 6.5 percent; pharmaceutical preparations 6 percent; and a variety of other consumer goods account for the rest. Amway's total sales topped $200 million in 1976, but Amway is still a small competitor compared to the giants that dominate the market in which it operates. The three largest firms in the soap and detergent market—Procter & Gamble, Lever Bros., and Colgate-Palmolive—account for over 80 percent of the total sales in that market. Procter & Gamble alone has about half these sales; in addition, it has about one-fourth of the total sales of personal care products. There are formidable barriers to entry into the market in which Amway operates; generally, a new competitor cannot enter at all unless it has very large amounts of money to spend on [3] advertising and promotion.[1] Amway skirted these near-insurmountable barriers and interjected a vigorous new competitive presence into this highly

[1] The three soap-and-detergent manufacturers mentioned above spent over $500 million in advertising and sales promotion in 1975. (Compare Amway's $200 million in sales.) Procter & Gamble alone—the largest advertiser in the United States—spent over $360 million in product promotion in 1975. Amway, by contrast, spent less than $1 million for advertising in 1975. Initial Decision, p. 68, Finding 175.

concentrated market by developing what is known as a "direct selling" distribution network.

B. Amway's Direct Selling Operation

Amway's products are the type usually sold in retail stores, especially in supermarkets. But Amway has totally avoided traditional retail outlets.[2] It retails its products directly to consumers on a "house-to-house" basis, using a sales force of about 360,000 independent distributors. Actually, Amway describes its retail marketing program as "person-to-person", since it encourages its distributors to seek out regular, repeat customers whom the distributors may service on an ongoing basis.

The advantages claimed for a direct selling operation include home delivery, explanation and demonstration of product characteristics and use, explanation of product guarantees, and other similar services. Amway has shown that these advantages can be considerable, as it has grown from sales of $4.3 million in 1963 to sales of over $200 million in 1976. One of the reasons for this rapid growth is that Amway's products have very high consumer acceptance. A marketing specialist called to testify at the hearings stated that Amway's laundry detergent, which has a very small market share and no national advertising, ranks third out of thirty-seven brands in brand loyalty. Other Amway products, including its automatic dishwasher detergent, detergent for fine clothing, bleach, rug cleaner, and laundry additives, each rank second in brand loyalty. Amway's liquid dishwashing soap led all sixteen brands surveyed in brand loyalty. [4]

C. Amway's Multilevel Distributor System

Each of the 360,000 Amway distributors is an independent businessperson. These distributors are governed in their relations with each other, with Amway, and, to some extent, with consumers, by the Amway Sales and Marketing Plan (the "Amway Plan").[3]

[2] Amway actually has a rule (in what is known as its "Rules of Conduct") which states that no Amway distributor shall permit Amway products to be distributed through any retail outlet. This rule, known as the "retail store rule," is discussed in greater detail at pages 21–23, *infra*.

[3] Generally speaking, the Amway Plan is a highly structured organizational outline, developed by VanAndel and DeVos to control the manner in which Amway products move through the distributor network to consumers. It is based on the "Code of Ethics and Rules of Conduct for Amway Distributors." The Amway Plan and the Code of Ethics and Rules of Conduct are set out in a manual, which Amway republishes every two to five years. The 1975 edition of the manual, which was current at the time of the hearings and is therefore frequently referred to herein is called the Amway Career Manual; some earlier editions, also referred to herein, were called the Amway Sale Plan.

Under the Amway Plan, a select few distributors known as Direct Distributors[4] purchase products at wholesale directly from Amway and resell the products both at retail to consumers and at wholesale to the distributors they personally "sponsored" (that is, the distributors they recruited). Each second-level distributor resells the products both at retail to consumers and at wholesale to the distributors he personally sponsored. The third-level distributors perform the same two functions. This multilevel wholesaling network ends with those distributors who have not sponsored any new distributors, and who make purchases from their sponsors solely for their own use or for resale to consumers. Thus there is beneath each Direct Distributor a "field" of distributors, each of whom receives products which have flowed through each level between himself and the Direct Distributor.[5] Amway directs that these [5] products, regardless of how many levels they pass through, are to be sold between distributors at the same prices the Direct Distributor paid for them.[6]

All distributors are encouraged to make retail sales and to sponsor new distributors who will themselves make retail sales; distributors earn money for successfully engaging in either of these activities. The way a distributor makes money on a retail sale is simple. Each time he makes such a sale, he keeps the difference between the retail price at which he sold the product and the wholesale price at which he bought it. The way a distributor earns money from sponsoring new distributors is more difficult to understand and requires a more lengthy explanation.

Under the Amway Plan, each distributor is eligible to receive a monthly "Performance Bonus" which is based on the total amount of Amway products he purchased that month for resale, both to consumers and to his sponsored distributors. This Bonus is basically a volume-based refund. The exact amount of the Bonus to be paid to a particular distributor is determined as follows. Each Amway product is assigned a "Point Value" (roughly corresponding to its wholesale cost) and a "retail value" (based on Amway's "suggested retail price" for that product). At the end of each month, a distributor adds up separately the total Point Value and the total retail value (referred to as his "Business Volume") for all the products he purchased that month from his sponsor (or, in the case of

[4] There were approximately 4000 Direct Distributors in 1977.

[5] Apparently some Direct Distributors have lines of sponsorship which are twenty to twenty-five levels deep. But of February 1977, approximately one-half of all Amway distributors either had a Direct Distributor as their sponsor were sponsored by a distributor who had a Direct Distributor as his sponsor. Over 70 percent of all distributors were the first three positions; over 85 percent were in the first four positions; over 93 percent were in the first five sitions; and roughly 99 percent were in the first seven positions.

[6] This restriction on wholesale pricing is discussed in greater detail at pages 12–13, *infra*.

a Direct Distributor, from Amway). He then computes the actual amount of his Performance Bonus by referring to the following "Performance Bonus Schedule," published by Amway:

IF YOUR TOTAL MONTHLY POINT VALUE IS:	YOUR PERFORMANCE BONUS IS:
7,500 or more points	25% of Your Business Volume
6,000 to 7,499 points	23% of Your Business Volume
4,000 to 5,999 points	21% of Your Business Volume
2,500 to 3,999 points	18% of Your Business Volume
1,500 ot 2,499 points	15% of Your Business Volume
1,000 to 1,499 points	12% of Your Business Volume
600 to 999 points	9% of Your Business Volume
300 to 599 points	6% of Your Business Volume
100 to 299 points	3% of Your Business Volume
less than 100 points	0% of Your Business Volume

[6] The Performance Bonuses are paid, in the first instance, by Amway to the Direct Distributors. Each Direct Distributor figures his Point Value and Business Volume for the month — both of which will include all the purchases he made from Amway to supply his own retail customers and to filter wholesale supplies down through the levels beneath him in his field or sponsorship — and is paid by Amway whatever percentage of his Business Volume he is entitled to. Each Direct Distributor is then responsible for paying out Performance Bonuses, from the amount he received from Amway, to the second-level distributors he sponsored.

The Direct Distributor usually will pay out less than he received from Amway, because these second-level distributors will each have a lower Point Value than he has, and they will therefore receive a lower percentage of their respective Business Volume amounts. For example, if five second-level distributors had each purchased a large enough volume of products in a month to be entitled to a 15 percent Performance Bonus, their Direct Distributor — in supplying their product needs as well as his own — would have purchased enough products from Amway to be entitled to a 25 percent Performance Bonus. The Direct Distributor would therefore be paid 25¢ by Amway on each dollar of his Business Volume, but he would only pay out 15¢ to his second-level distributors on each dollar of their respective Business Volumes. So the Direct Distributor would net a 25¢ Bonus on each dollar of Business Volume representing retail sales made by him to consumers, and a 10¢ Bonus on each dollar of Business Volume representing wholesale sales made by him to his sponsored distributors.

Each second-level distributor is then responsible for paying out

Performance Bonuses, from the amount the Direct Distributor pays to him, to the third-level distributors he sponsored. The second-level distributors will make money on the Business Volume generated by their sponsored distributors in the same way the Direct Distributors made money on the Business Volume generated by the second-level distributors; and so on, down through the successive levels of distributors.

This distribution hierarchy is not static, however, as any regular distributor, regardless of how many levels he may be below his Direct Distributor, may himself become a Direct Distributor by reaching a specified, high volume of purchases three months in a row.[7] When a regular distributor [7] qualifies as a Direct Distributor, he breaks out of the field of sponsorship he was in up to that time and begins to make his wholesale purchases directly from Amway. When a new Direct Distributor breaks out of his old position like this, he takes with him all those distributors he sponsored, all the distributors those persons sponsored, etc.[8]

D. Amway Distributors Association

The ADA is a trade association of Amway distributors.[9] Every Amway distributor is entitled to join the ADA, but only Direct Distributors may qualify as voting members. The voting members of the ADA meet once a year for a one-day meeting at which they elect nine of the eleven directors on the ADA Board. The other two directors — VanAndel and DeVos — are appointed by Amway. The Board performs three principal functions: it acts as a representative of the distributor association; it acts as an advisory board to Amway; and it acts as an arbitration board in disputes between distributors, or between Amway and a distributor.

II. The Alleged Violations

Complaint counsel have charged respondents with violations which fall into three categories. First, it is alleged that the Amway Sales and Marketing Plan is inherently deceptive, as it holds out the promise of "substantial income . . . as a result of . . . sales activities from . . . endless chain recruiting activities"; this is essentially a way of saying that the Amway Plan is an illegal pyramid scheme.

[7] *See* Initial Decision, p. 24, Finding 62, for a more exact statement of what is required.

[8] When a newly qualified Direct Distributor — who is by definition a very high volume performer — breaks out of his old place, it represents a great loss to the "old" Direct Distributor who previously funneled products to him. The old Direct Distributor is compensated by Amway for this loss by an additional monthly Performance Bonus consisting of 3 percent of the Business Volume of the new Direct Distributor.

[9] *See* Initial Decision, pp. 8-10, Findings 17-25, for a discussion of the history and origins of the ADA, and its relationship with Amway.

Second, it is alleged that various restrictions governing the sales, recruiting, and advertising activities of Amway distributors constitute unreasonable restraints of trade. Finally, respondents are charged with misrepresenting the profitability of a distributorship and the potential for recruiting and keeping new distributors. These charges will be taken up and discussed in order. [8]

A. Allegations That the Amway Plan Is a Pyramid Scheme

Complaint counsel argue that respondents have represented to prospective distributors that under the Amway Plan a distributor is likely to earn substantial income through a process of "multiplication" or "duplication", by recruiting others into the program who will themselves engage in recruiting, etc. Complaint counsel characterize the Amway Plan as "a scheme to pyramid by geometric growth layers of distributors." They state that "the Plan, by itself, is false, misleading and deceptive", because it leads to distributor saturation — that is, to such heavy concentration of Amway distributors that there is no one left to be recruited. The ALJ found that the record does not support these charges, and we agree.

The Commission had described the essential features of an illegal pyramid scheme:

> Such schemes are characterized *by the payment by participants of money to the company* in return for which they receive (1) the right to sell a product and (2) *the right to receive in return for recruiting other participants into the program rewards which are unrelated to sale of the product to ultimate users.* . . . As is apparent, the presence of this second element, recruitment with rewards unrelated to product sales, is nothing more than an elaborate chain letter device in which individuals who pay a valuable consideration with the expectation of recouping it to some degree via recruitment are bound to be disappointed. *In re Koscot Interplanetary, Inc.*, 86 F.T.C. 1106, 1180 (1975) (emphasis added), *aff'd mem., sub nom. Turner* v. *FTC* 580 F.2d 701 (D.C. Cir. 1978).

See also In re Ger-Ro-Mar, 84 F.T.C. 95 (1974), *aff'd in part, rev'd in part sub nom. Ger-Ro-Mar* v. *F.T.C.,* 518 F.2d 33 (2d Cir. 1975); *In re Holiday Magic, Inc.,* 84 F.T.C. 748 (1974). The Amway Plan does not contain the essential features described above, and therefore it is not a scheme which is inherently false, misleading, or deceptive.

The *Koscot, Ger-Ro-Mar,* and *Holiday Magic* cases all involved "marketing" plans which required a person seeking to become a distributor to pay a large sum of money, either as an entry fee (usually called a "headhunting" fee) or for the purchase of a large amount of nonreturnable inventory (a practice known as "inventory loading"). In exchange, the new distributor obtained the right to recruit others who would themselves have to pay a large sum of money — some of which would go to the recruiting distributor — to join the organization. [9]

By contrast, a person is not required to pay a headhunting fee or buy a large amount of inventory to become an Amway distributor. The only purchase a new distributor is required to make is a $15.60 Sales Kit, which contains Amway literature and sales aids; no profit is made in the sale of this Kit, and the purchase price may be refunded if the distributor decides to leave the business. Initial Decision, p. 12, Findings 34–37. Thus a sponsoring distributor receives nothing from the mere act of sponsoring. It is only when the newly recruited distributor begins to make wholesale purchases from his sponsor and sales to consumers, that the sponsor begins to earn money from his recruit's efforts. And Amway has prevented inventory loading at this point with its "buy-back rule," which states that a sponsoring distributor shall "[p]urchase back from any of his personally sponsored distributors leaving the business, upon his request, any unused, currently marketable products. . . ." By this rule, a sponsoring distributor is inhibited from pushing unrealistically large amounts of inventory onto his sponsored distributors in order to increase his Point Value and Business Volume, and thereby increase his Bonus.

Two other Amway rules serve to prevent inventory loading and encourage the sale of Amway products to consumers. The "70 percent rule" provides that "[every] distributor must sell at wholesale and/or retail at least 70% of the total amount of products he bought during a given month in order to receive the Performance Bonus due on all products bought . . . ." This rule prevents the accumulation of inventory at any level. The "10 customer" rule states that "[i]n order to obtain the right to earn Performance Bonuses on the volume of products sold by him to his sponsored distributors during a given month, a sponsoring distributor must make not less than one sale at retail to each of ten different customers that month and produce proof of such sales to his sponsor and Direct Distributor." This rule makes retail selling an essential part of being a distributor.

The ALJ found that the buy-back rule, the 70 percent rule, and the en customer rule are enforced, and that they serve to prevent iventory loading and encourage retailing. Initial Decision, p. 26, indings 72–75, and p. 58, Findings 145–47. Given these facts, the mway plan is significantly different from the pyramid plans ndemned in *Koscot, Ger-Ro-Mar,* and *Holiday Magic.* Specifically, e Amway Plan is not a plan where participants purchase the right to earn profits by recruiting other participants, who themselves are interested in recruitment fees rather than the sale of products. [10]

B. Distributor Restrictions

1. Direct Price-Related Restrictions

The ALJ found that Amway engaged in illegal resale price maintenance at both the wholesale and retail levels. Respondents argue before us that Amway merely suggests retail and wholesale prices. They argue there is no evidence in the record of current explicit agreements between Amway and its distributors, or of Amway enforcing its suggested prices through coercion of its distributors. What evidence of such conduct there is, they say, relates to acts and practices long since discontinued; and since there is no cognizable danger of a recurrence of these acts, they continue, an order prohibiting such acts is unwarranted. We reject respondents' arguments regarding Amway's wholesale and retail pricing practices, and affirm the ALJ's finding that Amway has engaged in illegal resale price maintenance.

As will be discussed below, evidence in the record conclusively demonstrates that Amway entered into explicit agreements with its distributors, in the past, regarding wholesale and retail pricing. And though Amway has discontinued the use of explicit agreements with respect to retail pricing, it still has explicit agreements with its distributors regarding wholesale pricing. Such explicit agreements to maintain resale prices are, of course, illegal per se. *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U.S. 373 (1911); *United States* v. *A. Schrader's Son, Inc.*, 252 U.S. 85 (1920); *cf. Schwegmann Bros.* v. *Calvert Distillers Corp.*, 341 U.S. 384, 386 (1951). After it discontinued the use of explicit agreements regarding retail pricing, Amway started out merely suggesting a retail price; but it then engaged in acts which secured adherence to its plan and thereby produced a "combination" or implied agreement, which had a direct and substantial effect on retail prices. *United States* v. *Parke-Davis Co.*, 362 U.S. 29 (1960); *Albrecht* v. *Herald Co.*, 390 U.S. 145 (1968); *In re Holiday Magic, Inc.*, 84 F.T.C. 748 (1974). Finally, Amway required its distributors to agree to certain other rules regulating the distribution and advertising of its products, which serve to bolster and effectuate its retail price maintenance scheme.

As to the practices it has relied on in the retail pricing area since it discontinued the use of explicit agreements, Amway seeks to rely on the *Colgate* doctrine. In *United States* v. *Colgate & Co.*, 250 U.S. 300, 307 (1919), the Supreme Court said: [11]

[T]he [Sherman Act] does not restrict the long recognized right of trader or manufacturer engaged in an entirely private business freely to exercise his own independent discretion as to parties with whom he will deal. And, of course, he may announce in advance the circumstances under which he will refuse to sell.

This language was interpreted to mean, as respondents state, in their Appeal Brief, at 12, that "a manufacturer [may] suggest resale prices for its products and independently . . . decline to do business with persons who resell the products at prices other than those suggested by the manufacturer." But cases decided since *Colgate* make it clear that the quoted language from that case was intended to create an exceedingly narrow exception. For example, in *United States* v. *Parke-Davis, supra,* the Supreme Court said:

An unlawful combination is not just such as arises from a price maintenance *agreement,* express or implied; such a combination is also organized if the producer secures adherence to his suggested prices by means which go beyond his mere declination to sell to a customer who will not observe his announced policy. 362 U.S. at 43.

Eight years later, in *Albrecht* v. *Herald Co., supra,* the Supreme Court raised the suspicions of many that *Colgate* was a dead letter when it stated that the *Colgate* exception might be exceeded if the sole evidence of a combination or conspiracy was that wholesalers and retailers, against whom a price maintenance plan was directed and enforced, had acquiesced in the plan. 390 U.S. at 150 n.6.

As will be developed in detail below, the evidence in this case establishes that Amway, in its efforts to secure adherence to its retail pricing plan, went far beyond the type of conduct that even a liberal reading of *Colgate* would allow. Specifically, Amway enlisted its distributors in a program designed to insure adherence to its stated pricing plan, and it structured certain of its Rules of Conduct so as to inhibit any kind of retail price competition among its distributors. Viewed against the background of the explicit agreements which Amway entered into in earlier years, these actions amply support a finding of illegal resale price maintenance. [12]

a. *Wholesale Prices*

Amway has illegally sought, and still seeks, to maintain its wholesale pricing policy through explicit agreement with its distributors. In a chapter of the 1975 Amway Career Manual[10] titled "The Amway Sales and Marketing Plan", Amway states: "[A distributor]

[10] *See* footnote 3 at page 4, *supra,* for a description of the Amway Career Manual.

cannot make money by simply selling products to his sponsored distributors because he sells them for the same price he paid for them: the distributor cost.[11]

Amway then converts this statement into a contractual provision by requiring a person seeking to become an Amway distributor to sign an application form which contains the following language:

> I agree to comply with the Amway Sales and Marketing Plan as set forth in official Amway Literature and manuals and to observe the spirit as well as the letters of the Amway Code of Ethics and Rules of Conduct. . . . I understand that my distriubtorship may be revoked if I fail to comply with the above provisions.[12]

[13] These explicit agreements are illegal *per se.*[13] *Dr. Miles Medical Co.* v. *John D. Park & Sons Co., supra.*

In addition, the "Distributor Order Form" (called an "SA-1"), which is published and circulated by Amway, instructs distributors to "consult the SA-13" for prices; an SA-13 is an Amway Wholesale Price List. Similarly, the 1975 Career Manual instructs distributors as follows: "Place your own order with your sponsor using the SA-1 Order Form. Use the Wholesale Price List to compute . . . Distributor Cost . . . for all items you have listed on the SA-1." Nowhere on any of these documents does it state that Amway's listed wholesale prices are "suggested" or "optional".

b. *Retail Prices*

In the retail pricing area, Amway originally used explicit agreements to prevent distributors from selling at less than Amway's specified retail price. In the 1963 Amway Sales Plan, the Rules of Conduct included the following rule: "No distributor shall sell

[11] Though worded differently at different times, the message has been the same down through the years. The 1963 Amway Sales Plan said: "[P]roducts sold between distributors are always sold at the same price, with no profit made on the immediate transaction. The profit is made later on the refund percentage." The 1968 Career Manual stated: "You sell Amway products to the distributor you sponsor at the same [price] at which you buy from your sponsor, and at which he buys from his sponsor."

[12] In the Career Manual itself, on the page facing the page containing the statement above about selling at distributor cost, Amway states:

> "[T]here is . . . . a binding contractual arrangement between Amway and its distributors, and that contractual arrangement is spelled out in detail not in a single printed document, but in a group of documents. Amway has always considered itself bound by a contract consisting of the following: . . . the Career Manual. . . ."

[13] As noted at page 5, *supra*, Amway does indicate in a " Performance Bonus Schedule" the percentage of a distributor's monthly Business Volume that he is to receive as a Bonus from his sponsor. If there were an agreement between Amway and its distributors at various levels that the distributors would adhere to this Schedule in paying out Performance Bonuses to the distributors they sponsored, it arguably would be an agreement with a substantial and direct effect on wholesale prices and would be illegal *per se. Cf. United States* v. *Socony-Vacuum Oil Co.*, 310 U.S. 150, 221 (1940). But there is no evidence that Amway or its distributors regard the Schedule as binding with respect to specific percentages. There is also no evidence that Amway enforces adherence to the percentages set out in the Schedule, nor even that most distributors do in fact adhere to those percentages. Findings 54 and 68 of the Initial Decision, at pp. 16, 25, indicate only that Amway enforces its rule that the Performance Bonuses it pays out to the Direct Distributors must be filtered through the distributor network, but not that the percentages Amway sets out are binding.

products sold under the Amway label for less than the specified retail price . . . ." Also included in this manual was a copy of the application a prospective distributor must fill out; each applicant was required to sign on the application underneath the following pledge: "I agree to observe the spirit as well as the letter of the Code of Ethics and Rules of Conduct of Amway Distributors." [14]

Respondents claim that the rule requiring adherence to Amway's retail prices was abolished in 1965. But as the ALJ pointed out, the record does not show that Amway has ever clearly told its distributors that they are free to set their own prices on retail sales to consumers.[14] Initial Decision, p. 87 n.12. Rather, it has signaled in several ways that it continues to regard fixed resale prices as being in everyone's mutual interest.[15]

Evidence presented at the hearing indicates that Amway has continued its efforts to secure compliance with its retail pricing policy long after it deleted the inculpatory language from its Rules of Conduct; in so doing, it has stepped well outside the protective parameters of *Colgate.* Specifically, it has invited its distributors to participate in a general scheme to detect and deter price cutting. For example, in a 1971 speech to a meeting of Direct Distributors,[16] DeVos was asked several questions by persons in the audience about what could be done with price cutters. He stated: [15]

> If you have a distributor who is selling Amway products at wholesale to a customer, our action has got to be first of all to get a complaint on it and find out who the distributor is that's doing it. Our next move has got to be to work on his removal, but this isn't an easy problem, because if this person wishes to sell to anybody on the street at whatever price he wants to, you're getting into some touchy areas on price-fixing. . . . Now you can try all the devious things you want to, to prevent this indiscriminate guy from price cutting . . . . [Y]ou can go ahead and delay shipments to him, you can berate him, you can lecture him. . . . Say [to him], "if you want to play price cutting game with your customers just let me know who they are because I make 25% and I'll go in and cut you right off. See, if its price cutting you want I'll show you how to play the game. Because I've got more money to play with than you have, haven't I?"[17]

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[14] Amway sends to distributors retail price lists for Amway products. The 1965 price list referred to the prices thereon as "retail". The 1970 price list used the phrase "retail prices (for sales tax purposes)". The current price list states that the prices listed are "suggested retail".

[15] In a 1970 copy of "The Amway Amagram" (a newspaper-like publication sent by Amway to its distributors), an article contained statements made by VanAndel to a meeting of Direct Distributors. He told them that Amway had conducted a test, in which it had divided the country into half, with prices set at normal levels in one half and at very high levels in the other half. He continued:

> "We wanted to see how much difference price would make in our marketing system. Actually, the sales volume per distriubtor in the higher price area was considerably higher than that in the other. I don't mean just 5% or 10%, I think it was over 50%. We concluded that higher price encouraged distributors to do more selling so he could make extra profit."

[16] This speech, along with several others, was tape-recorded live; the tapes of these speeches were admitted as evidence at the hearings.

[17] During this speech DeVos also said in regard to price cutting: "I can't do much about it. And I don't think you can do much about it." He added: "[Y]ou don't stand a legal chance of doing anything about it . . . . I can't

(Continued)

He went on in the same speech to caution the Direct Distributors to "guard against anything that's dog eat dog." He warned them that "price fixing is one of the things that the federal people and the FTC watch like a hawk," and advised them to talk to price cutters but not to write to them, because "when the FTC grabs that letter they'll say you're . . . price fixing." To say the least, the tactics recommended in this speech "go beyond mere announcement of [a] policy and [a] simple refusal to deal," and constitute "other means which effect adherence to [specified] resale prices." *United States* v. *Parke-Davis & Co., supra,* 362 U.S. at 44.

Similarly, Mr. Halliday — Amway's Executive Vice President and one of its three directors — told a meeting of Direct Distributors that if they learned of a distributor cutting prices, they should go to talk to that person's Direct Distributor and seek to persuade the price cutter to [16] stop. He added: "You're gonna have to work with him on an informal basis. As far as our being able to write him and saying 'You can't do it,' we cannot." This sounds far more like the invitation to acquiesce which the Supreme Court found unacceptable in *Parke-Davis* than the unilateral refusal to deal which might have some remaining vitality under *Colgate.*[18]

Amway has taken additional steps, beyond counseling Direct Distributors on how to deal with price cutters, to insure that price competition among distributors is thwarted. The clearest example of Amway's additional efforts to support its general price maintenance scheme is the "customer protection rule." This rule, which was included as one of the Rules of Conduct up until 1972, provides that each time an Amway distributor makes a sale to a retail customer, he obtains an exclusive right to re-sell to that customer for a thirty day period; if the distributor does make another sale to the customer within that period, he extends his exclusive right for another thirty days.

The ALJ found that the purpose and effect of the customer protection rule was to prevent price competition. Initial Decision, p. 89. This finding is supported by the obvious effect of the rule, and by Amway Vice President Halliday's statement that the purpose of the

take any action on it without endangering everybody in a federal restraint of trade activity." But these statements, essentially recognizing the dangerous legal problems that can arise from resale price maintenance and recommending caution in efforts at coercion, do not offset the clear meaning and effect of the other statements quoted above.

[18] Respondents rely heavily on *Knutson* v. *Daily Review, Inc.,* 548 F.2d 795 (9th Cir. 1976), *cert. denied,* 433 U.S. 910 (1977), for the proposition that where an explicit agreement is abandoned and is succeeded by strong recommendations of resale price maintenance, those recommendations do not constitute a "combination" in the absence of evidence of special coercion. But *Knutson* is not applicable here because Amway has gone far beyond "recommending": it has induced other distributors to assist in its program of detecting and deterring price cutting, and it has attempted to extract agreement and acquiesence from its distributors. *See* Initial Decision, pp. 39, 41-44, Findings 115, 117.

rule is "to prevent cut-throat competition" between distributors. Initial Decision, p. 88.

Respondents point to the fact that this rule was deleted from the Rules of Conduct in 1972; they claim this is evidence of discontinuance. However, in a speech to a meeting of Direct Distributors in 1974, Halliday reminded his listeners that the Golden Rule is the first rule in the Amway Code of Ethics[19] and then stated: [17]

> To what extent do you want to go in cutting out another Amway distributor? You have the absolute right to do it — the law says . . . there is no protection of customer under those circumstances. But you see, sometimes there's a — something above and beyond the law that you have to think about in terms of ethics.

Also, in the "Know-How Success Course", a training booklet used through 1974, sponsors are taught to test their recruits' knowledge of Amway policy with a quiz, which contains the following two questions (with their respective "right" answers):

> 9. Before you complete a sale to a new customer, is it important to ask if that customer is presently being serviced by another Amway distributor? YES or NO.
>
> - YES
>
> 10. As long as one distributor maintains exclusive right to resell a customer, no other Amway Distributor may sponsor that customer. TRUE or FALSE.
>
> - TRUE

These statements, coming as they did on top of an explicit rule in the recent past, undercut any argument of discontinuance.

In addition, Amway has tailored some of its otherwise reasonable Rules of Conduct to detect and prevent retail price cutting among distributors. An example is the ten customer rule (discussed at page 9, *supra*), which provides that a distributor must produce proof of retail sales to at least ten customers each month before he can receive his Performance Bonus. This rule has the reasonable purpose and effect of tying compensation to the retail sale of products. But it also serves as a detection device with regard to price cutting, because the "proof" a distributor must produce is a copy of the retail sales slip, which, by another rule, must "state the price charged". This aspect of the ten customer rule also has an obvious *in terrorem* effect on distributors who might be inclined to sell at less than Amway's "suggested" retail price. [18]

Two other rules currently included in the Rules of Conduct have had the effect of "shoring up" Amway's retail price fixing scheme.

[19] This literally is true, as the first provision of the Code reads: "I will make the 'Golden Rule' my basic principal of doing business. I will always endeavor to 'do unto others as I would have them do unto me.' "

The buy-back rule (discussed at page 9, *supra*) provides that a sponsoring distributor must buy back any products he sold to a sponsored distributor who has decided to go out of business. A 1973 Amway Legal Bulletin explained that one of the reasons for this rule is to insure that a distributor who is leaving the business does not "attempt to sell the products at a discount." *See* Initial Decision, pp. 44–46, Findings 120–23. The "fund-raising rule" provides that a distributor may sell certain Amway products in fund-raising drives held by church, service, civic or charitable organizations "provided such sales are made in accordance with the Amway Fund-Raising Plan." Under this plan (as it is described in the 1975 Career Manual), the selling organization only takes orders for the products; the orders are then turned over to an Amway distributor, who delivers the products, collects the purchase price, and pays an agreed-upon profit to the selling organization. Amway argues that the reason an Amway distributor is sent to deliver the product and pick up the purchase price is to allow the distributor to initiate contact with the purchaser. This argument might be convincing were it not for the history of this rule. The 1968 Amway Career Manual — which was distributed at a time when the charitable organization took sole responsibility for delivering the product and collecting the purchase price — gave the following advice to distributors supplying a fund-raising organization: "See that standard retail prices are observed. Do not permit cut-rate selling. Cut-rate selling during a fund-raising campaign could hurt your own regular selling of these items."

We do not say that the ten customer rule, the buy-back rule, and the fund raising rule are illegal in their entirety in this case. We do say that certain aspects of these rules, discussed above, as implemented here — with the plain purpose and effect of assisting in a program of illegal resale price maintenance — are illegal under Section 5 in that they contribute to a resale price maintenance program, *cf. National Society of Professional Engineers* v. *United States,* 435 U.S. 679, 692–93 (1978), and also that they are evidence of a purpose on the part of Amway to maintain an overall price maintenance program.[20] Initial Decision, p. 37, Finding 112. **[19]**

In a further effort to deter price competition, Amway has sought to prevent its distributors from advertising prices for Amway products.[21] Initial Decision, pp. 43–45, Findings 117, 119, 121. It has done

[20] The portions of the Final Order relating to rules (Order Paragraphs I.4, I.7, and I.8) are aimed solely at preventing their use in connection with the maintenance of retail prices; the Order does not otherwise disturb their operation.

[21] *See* pages 23–24, *infra.* for a detailed discussion of the advertising restrictions Amway has imposed on its distributors.

this by converting a series of restrictive advertising rules contained in its Rules of Conduct into contractual provisions,[22] and by terminating, or threatening to terminate, distributors who advertise Amway products at discount prices.[23] Besides contributing to Amway's overall scheme to control resale prices, this elimination of price advertising is a *per se* violation of Section 5. *See, United States* v. *Gasoline Retailers Asso., Inc.*, 285 F.2d 688, 691 (7th Cir. 1961); *United States* v. *The House of Seagram,* 1965 Trade Cases (CCH) ¶71,517, p. 81,275 (S.D. Fla. 1965); *cf. National Society of Professional Engineers* v. *United States,* 435 U.S. 679, 692–93 (1978). Moreover, this restriction on price advertising is evidence, along with the other price-related rules and practices discussed already, of Amway's intent to eliminate price competition in the retail sale of Amway products.

Finally, there is an additional, slightly different reason why Amway's retail pricing policy is illegal. This is not a situation, like *Colgate,* where a manufacturer is imposing its retail pricing policy on a corps of resistant, or even neutral, wholesalers and retailers. Rather, there is evidence that the ADA Board of Directors — which is the representative of Amway's distributors — agrees in advance with Amway on what the retail price of particular products is going to be. *See* Initial Decision, p. 27, Finding 79. In its Non-Profit Corporation Annual Report filed with the state of Michigan in 1975, the ADA stated that the "Purpose of the Corporation" was: "To act as a trade association for the purpose of setting policies with the company from whom purchases are made *and the pricing of all products sold direct to the consumer*" (emphasis added). Respondents have attempted to characterize this language as "inaccurate boilerplate". We find this characterization unpersuasive. [20]

c. *Respondents' Claims That Price Competition Does Exist*

Respondents argue that distributors do, in fact, demonstrate considerable independence and flexibility in wholesale and retail pricing. And several distributors (mostly Direct Distributors) who testified at the hearings were asked whether they were required by Amway to resell Amway products at a certain price, and answered "No". In addition, some of these distributors testified that they occasionally do sell for less than "suggested" retail or wholesale. However, as the ALJ observed, it is not surprising that out of a group

[22] *See* page 12, *supra*, for a discussion of how Amway converts the Rules of Conduct into a contract between Amway and each distributor.

[23] *See* Initial Decision, pp. 41–46, Findings 117, 119, 121, and p. 90. Also, Amway advises its distributors, in the Career Manual, that when a distributor violates one of the Rules of Conduct his Direct Distributor "may take such corrective action as he deems necessary, even terminating the violator's distributorship."

of 360,000 distributors, a few could be found who do "discount". Initial Decision, p. 88 n.13. The ALJ still found that the record showed that the vast majority of Amway distributors do not cut the retail price of Amway products. Initial Decision, p. 47, Finding 127. We agree with this finding.

Respondents also claim that substantial retail discounting is evidenced by the retail sales tax refunds Amway pays out to distributors. Amway collects retail sales tax, based on its suggested retail prices, from the Direct Distributors at the time it sells products to them wholesale; this is done at the request of state taxing authorities. *See* Initial Decision, p. 46, Finding 124. This sales tax is passed along in each wholesale sale of products, and is ultimately recouped at the time a product is sold at retail. Respondents point to the fact that a distributor may apply for a refund of some or all of this amount if he sells a product at less than Amway's suggested retail price. And in fact, respondents state, a large amount of money is refunded each month from Amway's sales tax collections. But complaint counsel point out that there are many reasons why a distributor could be entitled to a refund of some or all of the retail sales tax he paid, including: sales across state lines with different tax structures, sales to tax exempt organizations, and, most importantly, distributor home consumption.[24] Indeed, this "request-for-refund" policy could itself be ancillary to Amway's price maintenance plan if it were used as a means of learning which distributors have made sales at less than "suggested" retail. [21]

We conclude on the record that Amway has illegally sought to enforce its resale price policies, and, judging by market effects, has enforced them successfully throughout most of its distributor network.[25]

2. Other Challenged Distribution Restrictions

Complaint counsel also allege that two other Amway rules and restrictions — the "cross-group selling rule" and the "retail store rule" — violate Section 5 as unreasonable restraints of trade. The prohibition on cross-group selling, sanctified in Amway's Rules of Conduct, provides that a distributor must buy all his products from

[24] The ALJ found that home consumption of Amway products by distributors accounts for a significant amount of Amway's sales. *See* Initial Decision, pp. 55–56, Finding 137.

[25] Where a finding of resale price maintenance has been made, we routinely include in the order a provision prohibiting the use of suggested prices for some time after entry of the order. But in this case there are highly unusual circumstances which make the use of suggested resale prices not anti-competitive. Specifically, Amway has an unusual distribution system which relies on the sales efforts of hundreds of thousands of distributors, many of whom distribute Amway products part-time and are inexperienced in business matters generally. It is not unreasonable under these circumstances to give distributors some guidance in setting prices on the 150 products they try to sell.

his sponsor; by implication, a distributor may not sell Amway products to a person sponsored by someone else. The retail store rule — also one of the Rules of Conduct — provides that no distributor shall permit Amway products to be sold or displayed in "retail stores" or "other types of retail establishments, which are not technically stores, such as barber shops, beauty shops, etc."

Complaint counsel have characterized these restrictions as *per se* violations of Section 5, either as part of a plan to maintain prices, or as market division schemes horizontally imposed. We reject both these contentions. As to the price fixing charge, we have already found that Amway has entered into a series of express agreements and/or implied combinations with its distributors fixing wholesale and retail prices. There is no evidence on this record that the retail store rule or the cross-group selling rule were adopted to implement those vertical price fixing agreements, or that they contributed to that effect. If Amway's direct efforts at resale price maintenance are elimiated — as they should be through the order imposed here — there is no reason to believe resale price maintenance would persist as a reult of these two rules. [22]

If the restraints embodied in the cross-group selling and retail store rules were horizontally agreed to or induced, rather than vertically imposed by Amway on its distributors, the agreements would probably be illegal *per se* as horizontal divisions of market. *See United States* v. *Topco Associates, Inc.,* 405 U.S. 596 (1972); *United States* v. *Addyston Pipe & Steel Co.,* 85 F. 271 (6th Cir. 1898), *aff'd.,* 175 U.S. 211 (1899). Complaint Counsel claim that the ADA was formed before Amway, and that therefore the ADA must have been the source of all distributor restrictions. We do not find this approach conclusive on this question. Furthermore, the ALJ found that VanAndel and DeVos formed the ADA, at a time when they were distributing another manufacturer's products through a direct selling organization, in anticipation of starting their own manufacturing company. Initial Decision, pp. 8–10, Findings 17–25. Complaint counsel established that there is a constant dialogue between Amway and the ADA Board regarding the nature and consequences of the Amway Plan. But it does not follow that Amway is obligated to adopt, or does adopt, the recommendations or requests of the ADA Board when Amway is otherwise inclined to take different action or to take no action at all. It is likely that the dialogue exists primarily for the purpose of making the distributors — especially the Direct Distributors, who are linchpins in the Amway Plan — feel that they are an important part of the Amway organization and that their views and opinions are highly regarded. *See* Initial Decision, pp. 81–

82. Complaint counsel also point to the fact that VanAndel and DeVos, the two principal owners of Amway, are themselves the joint heads of a Direct Distributor organization. However, other than stating in their Appeal Brief, at 43, that the two men have "one of the largest Amway Direct Distributorships in the country," complaint counsel have provided no information or evidence on this point. All in all, we feel there is not sufficient evidence to support a finding that the Amway Rules of Conduct are not "essentially" vertical. Therefore they will be analyzed individually under the rule of reason. *Cf. Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36 (1977).

The cross-group selling rule, which applies only to distributors' wholesaling functions, was found by the ALJ to be "the basis for the Amway Sales and Marketing Plan":

It provides the structure by which products, information and compensation flow from Amway to the Direct Distributors and down to the distributors engaged in making the retail sale. It provides lines of communication and responsibility insuring that distributors are properly trained and [23] motivated and that consumers receive services provided under the Amway system of distribution. Used in conjunction with the performance bonus system, the cross-group selling rule gives sponsoring distributors an incentive to recruit, train, motivate and supply other distributors in order to gain a reward based on the sponsored distributors' sales volume. If sponsored distributors could buy Amway products from someone other than their sponsor, that incentive would not exist. Initial Decision, p. 100 (citations omitted).

We endorse this finding and conclude that the vertically imposed cross-group selling rule is reasonably ancillary to compensation, efficient distribution, and training. Given the large number of existing and potential distributors of Amway products, Amway's small size compared to its major competitors, and the direct relationship between the limitation on cross-group selling and the achievement of efficiencies within Amway's unique distribution system, we agree with the ALJ that the restriction is reasonable. *Continental T. V. Inc.* v. *GTE Sylvania, supra.*

The ALJ found that the retail store rule preserves Amway's direct-selling operation and consumer demand for Amway products, and provides an incentive to distributors to furnish special services to consumers:

Marketing experts gave credible testimony in this proceeding that if Amway products were sold in retail stores, distributors would lose interest in calling on consumers' homes, demonstrating and explaining products to create a demand which could be satisfied — perhaps at a lower price — at a retail store. Without a demand for the products, retail stores would soon lose interest in Amway products. Amway would then be faced with the necessity of creating demand in the traditional way of advertising expenditures and otherwise doing battle in the retail grocery stores, in a

> hostile oligopolistic marketplace. . . . The retail store rule gives Amway distributors an incentive to provide services to consumers and to create a consumer demand which would dissipate if Amway products were sold in retail stores. Amway distributors demonstrate and explain Amway products [24] and deliver to the consumer's home. These services are typically unavailable from retail stores. Because some Amway products are more concentrated than products sold in retail stores, demonstration and explanation are essential to consumer demand. Initial Decision, pp. 98–99 (citations omitted).

We endorse this finding as well. Since neither Amway nor any of its distributors can sell through retail outlets, this is not an instance where existing competition between different distributors or classes of distributors is being curtailed. Given Amway's small size (compared to its competitors), the plausible business reasons for the restrictions (relating mainly to Amway's ability to recruit distributors and induce them to provide special services), the absence of evidence that retail stores are excluded principally because of a belief that they would be price cutters, and the armies of distributors seeking to sell Amway products to all who wish to purchase them — we agree that complaint counsel has failed to show that this restriction is unreasonable.

3. Advertising Restrictions

Amway exercises a strong control over advertising by its distributors. It has placed especially severe restrictions on product advertising. One of the Rules of Conduct states: "No Amway distributor may produce or procure, from any source other than Amway, any literature relating to the Amway Sales and Marketing Plan or any Amway product." Thus the first rule on product advertising is that Amway has total control over what is actually said. Amway insists this restriction is necessary to protect its 125 registered trademarks and servicemarks, and to insure that its products are intelligently and consistently described.

Another rule provides that only Direct Distributors may advertise on radio, television, or in newspapers, and then only if they use ad mats and scripts obtained from Amway. Thus a distributor who is not a Direct Distributor may not advertise Amway products by any means other than hand- or mail-delivery of Amway sales aids and promotional materials. Amway claims it is reasonable to deny regular distributors the right to advertise products on radio, television, and in newspapers, because most distributors are inexperienced in business and tend to overestimate the effectiveness of advertising; if they were turned loose to advertise as much [25] and by whatever means they chose, many of them would unjustifiably increase their expenses to the point where they were driven from the market. In addition, respondents say, there is rapid turnover among distributors, and it would have a negative impact on Amway's image if consumers responded to ads placed by distributors who had since gone out of business.

The ALJ found these restrictions reasonable. Initial Decision, pp. 104–05. We concur in this finding, except that we find one aspect of Amway's restrictions on product advertising unnecessarily restrictive and ancillary to Amway's price maintenance scheme. Specifically, none of the Amway-designed sales aids, promotional literature, ad mats, or ad scripts provides a place for the advertising distributor to list his own retail price for the products advertised. And since no distributor may advertise Amway products other than by using the advertising materials designed and distributed by Amway, it follows that price advertising is effectively prohibited. To protect its servicemarkets and trademarks, Amway may — in reasonable ways that are not anticompetitive — prescribe the means by which distributors advertise products and the words they use; but Amway may not foreclose distributors from advertising product prices. *United States* v. *Gasoline Retailers Asso., Inc.,* 285 F.2d 688, 691, (7th Cir. 1961); *United States* v. *The House of Seagram,* 1965 Trade Cases (CCH) ¶71,517, p. 81,275 (S.D. Fla. 1965); *cf. National Society of Professional Engineers* v. *United States,* 435 U.S. 679 (1978).

Amway also restricts the use by distributors of the Amway name and logo on the exteriors of wholesale offices and automobiles, on checks, and in telephone directories. It restricts outdoor advertising on billboards or signs, and allows distributors to use the Amway name in classified recruiting advertisements only if the ads follow word-for-word one of seventeen formats provided by Amway. Finally, all Amway printed material is copyrighted and may not be reproduced by distributors without permission. The ALJ found these reasonable. *See* Initial Decision, pp. 32–35, Findings 94–108, and pp. 104–05. We question whether some of these restrictions are reasonably related to Amway's legitimate business needs; but we agree that complaint counsel have offered no plausible evidence from which we might conclude that the purpose or effect of these various restrictions is anticompetitive. [26]

C. Misrepresentations

Respondents were charged in the complaint with making false, misleading, and deceptive statements concerning the profitability of a distributorship. Specifically, complaint counsel claim respondents have affirmatively misrepresented distributors' earnings and recruiting potential, and have omitted material facts about business expenses and turnover among recruited distributors. Together, it is charged, these misrepresentations and omissions have the capacity to deceive distributors and potential distributors.

The different kinds of alleged misrepresentations involved are discussed in detail in the Initial Decision at pages 17–23 and 48–57. Most come from the 1975 edition of the Amway Career Manual, from the section advising a would-be sponsor on how to go about recruiting a new distributor. The method employed consists of explaining the Amway plan and appealing to the financial goals of the recruit. The ALJ found that, viewed in context, none of the statements challenged constitutes an illegal misrepresentation. Initial Decision, pp. 110–18. With the exception of those statements which make unrealistic earnings or sales claims, we affirm this finding.

The "non-earnings" claims made by Amway — which generally consist of vague references to the achievement of one's dreams, having everything one always wanted, etc. — are phrased in terms of "opportunity" or "possibility" or "chance"; and they are surrounded by warnings that hard work is required. We believe that these claims are primarily inspirational and motivational; to the extent that they dangle the likelihood of financial security and material success before the potential distributor, they constitute vague "puffs" which few people, if any, would take literally; and in any event, they are accompanied by appropriate qualifiers.

The same cannot be said, though, for certain statements and claims which contain references to specific dollar amounts which distributors are likely to earn. For example, in the 1975 Career Manual, Amway advises recruiting distributors to announce to persons they are trying to recruit that Amway offers an opportunity to "develop an income of as much as $1,000 per month." Amway also advises recruiting distributors to ask questions like the following:

> How much money per month do you need for that new car? $100 a month or more?
>
> What kind of home do you want — a three-bedroom ranch — with a price tag of $35,000–$40,000? [27]
>
> How much will it take to send the youngsters through college — $2,500 to $3,000 a year for each younster? If you could earn an extra $250 a month, you would have an additional $3,000 a year. This might be sufficient to send one youngster through one year of college.
>
> How much would you like as a continuing income — $100 a month?

But not all of Amway's recommended recruiting claims are so generalized. At one point in the Career Manual it states: "If you make 'two sales a day . . . the Amway way' on each of 20 days per month, your retail sales can easily amount to $200.00 per month even though you work less than an hour per day." The Manual uses this $200 figure again when it instructs a recruiting distributor on how to "draw the circles" — a device used to explain the way a distributor earns a Performance Bonus off the purchases made from him by the distributors he has sponsored. He is advised to state: "Let's say, for example, that you sponsor six distributors and that each one of these distributors starts his own retail business selling $200 a month." He then draws a big circle, representing the sponsor, and six smaller circles, each of which represents a sponsored distributor. The figure $200 is written into each of these six smaller circles to indicate that each sponsored distributor has a Business Volume of $200 per month. The recruiting distributor then does a series of calculations showing the Performance Bonus the sponsor will earn as a result of having six sponsored distributors with individual monthly Business Volumes of $200. In the example of this diagram included in the Career Manual, the following language is placed above the circles: "For discussion purposes, let's round out the numbers to $200.00. I'm sure you realize that some will do much less and some more. But, if they make two sales a day, they should sell at least $200 (at BV) per month." But in spite of this prominent disclaimer, the impression is created that $200 is a typical or average monthly Business Volume.[26] [28]

In fact, the record shows that in 1969–70 the average monthly Business Volume of Amway distributors was about $20, and in 1973–74 it was about $33.[27] Initial Decision, pp. 55–56, Finding 137. And while some Direct Distributors do have annual Business Volumes in the thousands of dollars, they are less than 1 percent of Amway's 360,000 distributors. Initial Decision, p. 50, Finding 133. Thus the claims of incomes of $100 to $1,000 per month and the use of the $200 figure in such a way as to imply that it is a typical monthly retail sales figure, constitute misstatements of the amount of money a distributor is likely to earn. The $200 Business Volume figure

[26] "What impression is made by a given practice is a question of fact for the Commission to determine . . . ." *Benrus Watch Co.* v. *FTC*, 352, F.2d 313, 318 (8th Cir. 1965), *cert. denied*, 384 U.S. 939 (1966); *accord Niresk Industries, Inc.* v. *FTC*, 278 F.2d 337, 342 (7th Cir.), *cert. denied*, 364 U.S. 883 (1960); *Kalwajtys* v. *FTC*, 237 F.2d 654, 656 (7th Cir. 1956), *cert. denied*, 352 U.S. 1025 (1957).

[27] We note that this figure is not "retail sales", but Business Volume — that is, the retail value of the products purchased for resale to consumers and sponsored distributors, and for distributor home consumption, which was stated before, constitutes a large portion of all sales of Amway products. *See* Initial Decision, pp. 55–56, Finding 137.

overstates the true average Business Volume by more than 500 percent.[28] And the often unqualified claims regarding actual income are even more removed from reality, at least as reality exists for the vast majority of Amway distributors.

The Commission previously addressed issues concerning unrepresentative earnings claims in *National Dynamics Corp.,* 82 F.T.C. 488 (1973), *aff'd in part and rev'd. in part,* 492 F.2d 1333 (2d Cir.), *cert. denied,* 419 U.S. 993 (1974). In *National Dynamics,* respondents were manufacturers of a battery additive which they marketed through 12,000 distributors. In attempting to recruit new distributors, respondents made generalized earnings claims like, "You can earn $12,000 a year. . . .", and "What do you want to make of your life? . . . An income of $15,000 to $50,000 per year?" They also quoted the following earnings for named individuals: "$1,554 one week", "$148 one day", "$2,316.96 one week", "$1,028 one month". The Commission opinion noted that of the 12,000 [29] distributors selling for respondents in 1969, not more than sixty, or one-half of 1 percent of the total number of distributors, made profits in excess of $10,000. *Id.* at 563. Based on this fact, the Commission found the generalized earnings claims to be misleading and deceptive because they "far exceed[ed] the earnings normally received by dealers." *Id.* at 565. The specific earnings claims for named individuals were also found to be misleading and deceptive because they had "the capacity and tendency to lead members of the public to believe that a substantial number of distributors will regularly earn such amounts." *Id.* at 564.

Amway's specific earnings and sales claims are similar to the claims in *National Dynamics:*[29] they far exceed the amounts normally received by distributors, and, in their cumulative impact, they have the capacity and tendency to lead potential distributors to believe that a substantial number of distributors really do receive such amounts. Therefore, they constitute illegal misrepresentations under Section 5.[30]

Finally, the ALJ found, contrary to complaint counsel's charges, that Amway has not misrepresented distributors' recruiting poten-

[28] In a speech given to Direct Distributors in 1974, DeVos stated that the reason for using a figure as large as $200 is to raise distributors' "vision" of their own potential. *See* Initial Decision, p. 55, Finding 136. But this does not change the fact that the $200 figure overstates the true average Business Volume amount; and a statement need not be intended to deceive in order to have the capacity to deceive.

[29] It should be noted, though, that Amway has not advertised specific earnings of named individuals. In fact, the 1975 Amway Career Manual states: "Don't quote dollar incomes on specific individuals even though you may want to use their stories about the homes in which they live, the cars they drive, or the airplanes they fly."

[30] We note here that complaint counsel have attacked earnings claims made to potential distributors and to persons who already were Amway distributors. We restrict our finding of a violation to those earnings misrepresentations made to potential distributors. We believe that experienced distributors can be expected to be aware of the opportunities, or lack of opportunities, open to them under the Amway Plan. Statements of the kind discussed in the Initial Decision, at p. 49, Finding 132, when made to persons who already are distributors, can be considered "inspirational" in nature.

tial, and that it has not failed to disclose that distributors incur expenses in operating their distributorship, or that there has been a high rate of turnover among newly recruited distributors. *See* Initial Decision, p. 57, Findings 140–41. We affirm this finding. [30]

III. Procedural Issues

Respondents claim that numerous procedural errors and irregularities occurred, to their prejudice, during this proceeding and the investigation which preceded it. First, they claim that no cease and desist order can be entered against them because part or all of the evidence supporting the complaint may have been acquired by unlawful means. Respondents moved to dismiss the complaint on the same grounds in April 1975. The Commission denied that motion but stated that its ruling was without prejudice to any attempts by respondents to move the ALJ to suppress evidence they claim was improperly obtained. The ALJ thereafter took steps to monitor the source of witnesses and exhibits complaint counsel proposed to call or introduce at the hearings. We find, upon review, that the steps taken by the ALJ were adequate and effective.

Next, respondents claim they were prejudiced by the ALJ's denial of their request for discovery from the files in *Colgate-Palmolive, et al.,* Commission File No. 741–0048 (relating to a non-public FTC investigation). Respondents argue that the discovery sought from that file relates to entry barriers and concentration in the soap and detergent industry, and that it could provide proof of the reasonableness of the vertical restrictions in the Amway Plan. We reject respondents' argument that they were entitled to discovery from this file and affirm the ALJ's order denying discovery.[31]

Respondents further state that a series of procedural errors and irregularities are set forth in a motion to dismiss read into the record on the first day of trial. Though that motion was denied by the ALJ in a June 15, 1978 Order, respondents state that they continue to assert the positions set forth in the motion. Without describing the alleged errors and irregularities, they add: "The bases for those positions are set forth in respondents' motion and do not require repetition here." We have considered the motion set forth in the transcript, and we affirm the ALJ's decision to deny. [31]

Finally, respondents assert that the transcript of testimony given at the hearings is full of errors, and that the record must either be

[31] We note that all of the vertical restrictions challenged have been found to be reasonable, except as they were ancillary to Amway's illegal resale price maintenance plan. We also note that these findings were based on our view that the product markets in which Amway competes are indeed concentrated, and that Amway's presence has had some procompetitive consequences.

reopened to allow correction of these errors or the complaint must be dismissed. Respondents filed a veritable blizzard of papers on this matter with the ALJ, who issued more than ten Orders in response. A brief description of the events leading to respondents' objection is appropriate.

Soon after the hearings ended, respondents objected to about 2000 pages of the transcript, claiming they contained errors. Complaint counsel objected to additional pages, and the parties filed with the ALJ a stipulation of corrections involving over 2000 pages of the transcript. In Orders issued on December 6 and December 30, 1977, and January 6, 1978, the ALJ noted that almost all these stipulated changes involved typographical or spelling errors, and ordered the parties to specify the errors affecting substance. This was to insure compliance with Section 3.44(b) of the FTC Rules of Practice, which says that "[c]orrections of the official transcript may be made only when they involve errors affecting substance . . . ." After considerable maneuvering by the parties with respect to what constitutes an error of substance, the ALJ issued an order on January 24, 1978 stating:

> Respondents submit that there should be changes made on almost 2000 pages of the transcript in this case . . . . Respondents argue that errors in spelling of some of the key words in the transcript must be corrected for the purpose of accuracy in their computer retrieval system. This is a convincing argument. I therefore hold that the pages of the transcript enclosed with this order shall be corrected by the official reporter pursuant to Rule 3.44(b).

By letter of March 13, 1978, the official reporter responded, stating that all the requested changes had been made and characterizing them as "errors in spelling" and "changes in grammer or syntax, post-hearing selections of synonyms deemed more appropriate, expressions of parentheticals in the form of commas, and in some instances complete changes in the sentence structure which reflects the desire of witnesses, after the fact, to communicate their thoughts in clearer fashion." [32]

Still not satisfied, respondents moved, during an oral argument on the merits of the case, to dismiss the complaint on the grounds that not all the ordered corrections had been accomplished.[32] In reply, complaint counsel informed the ALJ that they had learned from the official reporter that no one had arranged to have the transcript put into computer readable form such that it could be utilized in a computerized information retrieval service. This led the ALJ to remark, in his June 15, 1978 Order denying the motion to dismiss,

[32] Respondents assert on appeal that ordered corrections have still not been made on 350 pages, and that there are 35 "garbled or omitted portions of the transcript".

that the 2000 pages previously ordered corrected "need not, therefore, have been retyped pursuant to Rule 3.44(b)." The ALJ continued: "[R]espondents have not been able to point to one proposed finding which might be affected by any of the errors in the transcript they allege." The ALJ noted that the parties were in agreement as to every correction ordered, and therefore instructed complaint counsel to have the stipulation of changes — which consists of hand corrected copies of the transcript pages in question — inserted in the record. Complaint counsel did so, and the hand-marked pages are included in the record as "ALJ Exhibit A". We interpret the ALJ's statement above — that none of the remaining "errors" affects any proposed finding — to mean that none of those errors affect substance. Therefore, no further corrections of the record need be made (if, indeed, any ever did need to be made).

IV. Conclusions

We conclude that respondents have agreed and combined with each other and/or with Amway distributors to fix the resale prices of Amway products, at both the wholesale and retail levels, in violation of Section 5 of the Federal Trade Commission Act. Respondents have also made earnings and sales claims which have the capacity to deceive the potential distributors to whom they have been made; this too, is in violation of Section 5. We have decided that it is appropriate and necessary to order respondents to cease and desist from these violations, and from certain offenses reasonably related to them.

The Commission has also concluded that complaint counsel have failed to establish that respondents have engaged in the other alleged violations of Section 5. Therefore those charges against respondents are dismissed.

Final Order

This matter having been heard by the Commission upon the cross-appeals of respondents and complaint counsel from the Initial Decision, and upon briefs and oral argument in support thereof and opposition thereto, and the Commission for the reasons stated in the accompanying Opinion having determined to affirm in part and reverse in part the Initial Decision:

It is ordered, That the Initial Decision of the administrative law judge be adopted as the Findings of Fact and Conclusions of Law of the Commission, except to the extent inconsistent with the accompanying Opinion.

Other Findings of Fact and Conclusions of Law of the Commission are contained in the accompanying Opinion.

It is further ordered, That the following Order to Cease and Desist be, and it hereby is entered: [2]

I

It is ordered, That respondents Amway Corporation and Amway Distributors Association, and their officers, agents, employees, representatives, members, successors and assigns, and respondents Jay VanAndel and Richard M. DeVos, individually, and their agents, employees, and representatives, directly or indirectly through any corporate or other device, in connection with the offering for sale, sale, or distribution of cleaning or personal care products, or any other products or goods in commerce, as "commerce" is defined in the Federal Trade Commission Act, shall forthwith cease and desist from:

1. Fixing, establishing, or maintaining, or attempting to fix, establish, or maintain, the price at which any distributor sells or offers for sale any product at wholesale or retail.

2. Stating that distributors are required to, or do, charge a particular price in wholesale or retail sales of any product.

3. Entering into any contract, agreement, understanding, or arrangement with any distributor which fixes, establishes, or maintains the price at which that distributor sells or offers for sale any product at wholesale or retail.

4. Taking any action, or counseling any distributor to take any action, designed to detect the price at which any distributor sells or offers for sale any product at wholesale or retail, including but not limited to: requiring distributors, in proving that they made retail sales to ten different persons in a month, to disclose the price at which they made such sales; directing or requesting any distributor to report to his Direct Distributor, to Amway, or to any other person or entity, knowledge he or she has of another distributor selling products at a price different from Amway's suggested wholesale or retail price; or allowing the price information submitted by any distributor seeking a full or partial refund of amounts paid by him or her for state retail sales tax, to be seen by any person other than those responsible for paying out such refunds, or to be used for any purpose other than paying out such refunds.

Provided, however, it shall not be a violation of this order for Amway to receive information about the price a distributor charged in a particular retail sale if such information is received by Amway solely as a result of such [3] sale being one of the following types: (1)

a sale wherein the purchaser used a bank credit card in making the purchase; (2) a sale of catalog merchandise wherein the purchaser paid by personal check payable to Amway; or (3) a sale to a commercial account wherein Amway financed the purchase.

5. Taking any action, or counseling any distributor to take any action, designed to deter distributors from selling or offering for sale products at a price different from Amway's suggested wholesale or retail prices, including but not limited to: addressing communications regarding price to any individual distributor, rather than to distributors as a class; delaying, or threatening to delay, the shipment of products to any distributor; withholding, or threatening to withhold, any distributor's Performance Bonus, if such distributor is otherwise entitled to such Bonus; underselling, or threatening to undersell, any distributor in retaliation for such distributor having sold or offered to sell products at a price different from Amway's suggested wholesale or retail prices.

6. Preventing or discouraging, or attempting to prevent or discourage, any distributor from selling or offering for sale products at retail to any person or entity, on the grounds that such person or entity is the customer of another distributor.

7. Requiring a distributor who is terminating his relationship with Amway to sell his remaining products back to Amway or to another distributor; *provided, however,* it shall not be a violation of this order to give a distributor who is terminating his relationship with Amway the opportunity to sell his remaining products back to Amway or another distributor.

8. Preventing, or attempting to prevent, a fund raising organization from selling or offering for sale products at a price different from Amway's suggested retail price.

9. Preventing, or attempting to prevent, distributors from advertising the prices at which they are selling or offering for sale products, including but not limited to, failing to include a place for distributors to disclose price in any existing or future sales aids, promotional literature, advertising mats, advertising scripts, etc., used by distributors in advertising Amway products. [4]

10. Publishing or distributing, directly or indirectly, any wholesale or retail price list, order form, promotional material, or any other document which lists resale prices for products without stating clearly and conspicuously thereon: "The prices stated here are suggested prices only. Distributors are not obligated to charge these prices. Each distributor is entitled to determine independently the prices at which products may be sold to other distributors or to consumers."

II

It is further ordered, That the aforesaid respondents and their officers, agents, employees, representatives, members, successors, and assigns, directly or indirectly, in connection with inducing or seeking to induce the participation of any person in any distribution, sales, or marketing plan, in commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. Misrepresenting in any manner the past, present, or future profits, earnings, or sales from such participation.
2. Representing, by implication, by use of hypothetical examples, or otherwise, that distributors earn or achieve from such participation any stated amount of profits, earnings, or sales in excess of the average profits, earnings, or sales of all distributors in any recent year respondents may select, unless in conjunction therewith such average profits, earnings, or sales is clearly and conspicuously disclosed, or the percent of all distributors who actually achieved such stated profits, earnings, or sales in such year is clearly and conspicuously disclosed.

III

It is further ordered, That respondent Amway Corporation or its officers, agents, representatives, employees, successors or assigns shall, within thirty (30) days from the effective date of this order, deliver a copy of this order to all persons who are currently Amway distributors.

IV

It is further ordered, That respondents and their successors and assigns notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondents such as dissolution, assignment or sale resulting in the emergence of successor corporations, the creation or dissolution of subsidiaries, or any other change in the corporations or in the Amway Sales and Marketing Plan which may affect compliance obligations arising out of the order. [5]

V

It is further ordered, That the respondents herein shall within sixty (60) days from the effective date of this order, file with the Commission a report in writing setting forth in detail the manner and form in which they have complied with this order.

IN THE MATTER OF

INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMEN AND HELPERS OF AMERICA, LOCAL UNION 959

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2963. Complaint, May 9, 1979 — Decision, May 9, 1979

This consent order, among other things, requires an Anchorage, Alaska labor union local to cease entering into agreements or understandings which restrict signatory construction companies to deal only with subcontractors who agree with the same terms and conditions binding between the union and the contractors. Additionally, the order prohibits the local from taking any action that would discriminate or economically injure non-compliers.

Appearances

For the Commission: *Stevan D. Phillips.*

For the respondent: *George H. Davies,* Seattle, Wash.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that the above-named respondent has violated Section 5 of the Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PAR. 1. The International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America, Local Union 959 (hereinafter sometimes referred to as "respondent" or "Local 959") is an unincorporated labor association, with its principal office and place of business located at 1200 Airport Heights Road, Anchorage, Alaska. Membership of respondent consists of approximately 15,000 individuals who are engaged as employees in various occupations in Alaska.

PAR. 2. Respondent now and for some time last past, has been engaged in the representation of its members, including the conduct of negotiations and execution of agreements with various employers engaged in the construction businesses. In the course of its activities, respondent has engaged in various acts and practices which are in or affecting interstate commerce, within the meaning of the Federal Trade Commission Act.

PAR. 3. Respondent has agreed with certain employers engaged in the construction business, including members of the Alaska Chapter of the Associated General Contractors of America, Inc. to prevent or hinder competition among subcontractors or contractors. Such agreements provide, for work within the jurisdiction of respondent, that:

A. the employer engaged in the construction business shall not subcontract any work, except to subcontractors who agree to perform the work in accordance with all the terms and conditions of the agreement;

B. the employer engaged in the construction business shall assure that subcontractors become signatory to the agreement before the subcontractors perform any work for the business;

C. members of the bargaining unit represented by respondent shall not perform any work for other employers engaged in the construction business, except in accordance with the terms and conditions of the agreement.

PAR. 4. As a result of these agreements, subcontractors are foreclosed from or restricted in competing for work offered by employers engaged in the construction business having such an agreement with respondent.

PAR. 5. The aforementioned acts and practices constitute unfair methods of competition in violation of Section 5(a) of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and respondent having been furnished thereafter with a copy of a draft of complaint which the Seattle Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty days, and having duly considered the comments filed thereby by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

A. Respondent International Brotherhood of Teamsters, Chauffeurs, Warehousemen, and Helpers of America, Local Union 959 is an unincorporated labor association existing and doing business in the State of Alaska, with its office and principal place of business located at 1200 Airport Heights Road, Anchorage, Alaska.

B. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

It is ordered, That respondent International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America, Local Union 959, its successors and assigns, affiliated sub-divisions, officers, trustees, employees, agents and members, directly or indirectly through any other form of business organization, shall forthwith cease and desist from:

1. Entering into any agreement or understanding that requires an employer engaged in the construction business to use or deal only with third party businesses who agree to perform work on the same terms and conditions as are agreed to between such employer engaged in the construction business and respondent;

2. Entering into any agreement or understanding with an employer engaged in the construction business that requires a third party business to be signatory to a collective bargaining agreement or other type of agreement that is binding between respondent and such employer engaged in the construction business;

3. Entering into any agreement or understanding with an employer engaged in the construction business that requires respondent to agree to the same terms and conditions of employment with a third party business as are binding between respondent and such employer engaged in the construction business;

4. Taking any action which would discriminate against or

economically injure those employers engaged in the construction business which deal with third party businesses on terms other than those agreed to between such employer engaged in the construction business and respondent.

Provided, however, That respondent shall not be prohibited from engaging in any legal activity now or later authorized by federal labor law such as the right of respondent to engage in standards picketing, or entering into any agreement authorized by §8(e) of the National Labor Relations Act, 29 U.S.C. 158(e), as long as said agreement is only effective when a member of the bargaining unit represented by respondent is employed and currently working at the site of the construction, alteration, painting or repair of the building, or other work.

It is further ordered, That respondent deliver a copy of this order to each of its present business agents, officers, trustees, and labor negotiators, and secure from each such person a signed statement acknowledging receipt of said order and that respondent, for a period of three (3) years subsequent to the date of this order, deliver a copy of this order to future business agents, officers, trustees and labor negotiators and secure from each such person a signed statement acknowledging receipt of such order.

It is further ordered, That respondent's Secretary-Treasurer, for a period of three (3) years subsequent to the date of this order annually furnish to the Federal Trade Commission any collective bargaining agreements with any employer engaged in the construction business.

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the organizational status of the respondent such as dissolution, assignment or sale resulting in the emergence of a successor labor organization, or any other change in the respondent which may affect compliance obligations arising out of the order.

It is further ordered, That the respondent herein shall within sixty (60) days after service upon it of this order, file with the Commission a report, in writing setting forth in detail the manner and form in which respondent has complied with this order.

IN THE MATTER OF

ALUMINUM COMPANY OF AMERICA, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2964. Complaint, May 11, 1979 — Decision, May 11, 1979

This consent order, among other things, requires a Pittsburgh, Pa. producer of aluminum building products and its subsidiary, Alcoa Building Products, Inc., to cease disseminating or participating in the dissemination of advertisements which contain fuel reduction, heat loss reduction, energy savings or thermal insulation representations regarding residential aluminum siding. The order also requires that the R-value for insulating material be disclosed in advertisements which merely use the term "insulated aluminum siding" for descriptive purposes.

Appearances

For the Commission: *David W. Plottner.*

For the respondents: *Russel W. Porter, Jr.,* Pittsburgh, Pa.

COMPLAINT

The Federal Trade Commission, having reason to believe that Aluminum Company of America, a corporation, hereinafter sometimes referred to as Alcoa, and Alcoa Building Products, Inc., a corporation, hereinafter sometimes referred to as ABP, have violated the provisions of Section 5 of the Federal Trade Commission Act and that a proceeding by it in respect thereof would be in the public interest, issues this complaint:

PARAGRAPH 1. Respondent Alcoa is a Pennsylvania corporation with its principal office at 1501 Alcoa Building, Pittsburgh, Pennsylvania. It dominates and controls the acts and practices of Alcoa Building Products, Inc.

Respondent Alcoa Building Products, Inc. is a Pennsylvania corporation wholly owned and operated by Alcoa as its subsidiary, with its principal office at 1200 Two Allegheny Center, Pittsburgh, Pennsylvania.

PAR. 2. Respondent Alcoa, a leading producer and fabricator of aluminum, is now, and has been, engaged in the advertising of aluminum building products, including, but not limited to, residential aluminum siding distributed and sold by its wholly-owned subsidiary, ABP.

Respondent ABP is now, and has been, engaged in the distribution, advertising, and sale of aluminum building products, including residential aluminum siding.

PAR. 3. Respondents maintain, and at all times mentioned herein have maintained, a substantial course of trade in the distribution, advertising, including that referred to in Paragraph Four, and sale of the aforementioned products in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. Through the use of advertisements and other printed materials, respondents have made statements with regard to their residential aluminum siding. Among said statements are the following:

(a) When properly applied over reflective aluminum foil in your present exterior siding, Alcoa siding forms a protective insulating envelope that could reduce heat loss in winter and heat gain in summer. And save precious fuel.

(b) Home insulation can be beautiful.

(c) Alcoa aluminum siding: the beautiful insulator.

(d) Not so apparent are the long term fuel savings possible with Alcoa siding, but you'll know they're there when you take a look at the amount you can save after installation.

(e) As you can see, the hypothetical Wellingtons and Hamiltons saved a considerable amount of fuel after they had Alcoa siding installed.

(f) YOUR HOUSE CAN HIT BACK WHEN THE ENERGY CRISIS HITS HOME. Alcoa building products can help your house put the crunch on energy consumption. One example is Alcoa siding.

(g) Alcoa insulated siding saves on heating and cooling costs! Save on fuel bills at your house like never before! That's right Alcoa insulated siding helps insulate your home year round.

(h) You'll probably use less fuel in years to come because Alcoa siding has definite insulating advantages.

(i) You can beautify your home and insulate it at the same time with Alcoa siding.

(j) We sell insulation in 17 colors, 5 textures and 50 states. From Alaska out to Hawaii, around to Florida and up to Maine, Alcoa Building Products can do a beautiful job of insulating against both cold and heat. . . .

PAR. 5. By the use of the statements described in Paragraph Four, and others of similar meaning, respondents have represented, directly or by implication, that:

(a) Aluminum siding installed over aluminum foil, using prevalent and accepted installation methods, has significant insulation value and will insulate pre-existing homes, thereby significantly saving energy and reducing fuel costs.

(b) The purchase of aluminum siding, regardless of type, and its subsequent installation on pre-existing homes, regardless of method of installation, is a meaningful, valuable, significant, or economical way: to insulate an older home, or to cut heat loss through the exterior walls of an older home, and, accordingly, to save energy and reduce fuel bills.

PAR. 6. In fact:

(a) (1) Plain aluminum siding installed over aluminum foil has little or no insulation value, and will not insulate pre-existing homes, thereby significantly saving energy and reducing fuel costs.

(2) Insulated aluminum siding installed over aluminum foil in pre-existing homes using prevalent and accepted installation methods frequently provides no or little insulation value, and does not result in substantial reductions in energy use and fuel costs.

(b) The purchase of aluminum siding, regardless of type, and its subsequent installation, on pre-existing homes, regardless of method of installation, is not a meaningful, valuable, significant, or economical way: to insulate an older home, or to cut heat loss through the exterior walls of an older home, and, accordingly, to save energy and reduce fuel bills.

Therefore, the statements and representations set forth in Paragraphs Four and Five were, and are, false, misleading, and deceptive practices.

PAR. 7. In the course and conduct of their business, and at all times mentioned herein, respondents have been, and now are, in substantial competition in commerce with corporations, firms, and individuals engaged in the sale of residential aluminum siding.

PAR. 8. The use by respondents of the aforesaid deceptive and unfair practices has had, and now has, the tendency and capacity to mislead and deceive a substantial portion of the purchasing public into the purchase of substantial quantities of respondents' products. Therefore, these practices were and are to the prejudice and injury of the public and constitute unfair or deceptive acts or practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Cleveland Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by the respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Aluminum Company of America is a corporation organized, existing and doing business under and by virtue of the laws of the Commonwealth of Pennsylvania with its office and principal place of business located at 1501 Alcoa Building, Pittsburgh, Pennsylvania.

Respondent Alcoa Building Products, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the Commonwealth of Pennsylvania, with its offices and principal place of business located at 1200 Two Allegheny Center, Pittsburgh, Pennsylvania.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding, and of the respondents, and the proceeding is in the public interest.

ORDER

For purposes of this order, the following definitions shall apply:

"Advertisement" means any written or verbal statement, illustration or depiction, whether the same appears in a television or radio broadcast, newspaper or newspaper supplement, magazine or magazine supplement, label, brochure, leaflet, circular, mailer, book insert, journal, catalog, sales promotion material, other periodical literature, billboard, public transit card, point of purchase display, or in any other media.

"Representation" means any direct or indirect statement, suggestion or implication.

"R Value" is the numerical measure of the degree of thermal resistance of a particular material.

For the purposes of this order the disclosed R Value shall be the R Value, expressed to the nearest tenth, of the thickness of respondents' product as packaged and shall be determined by actual tests of respondents' product. The tests shall be based on competent, widely accepted, scientific, engineering criteria, applicable to a retrofit situation.

It is ordered, That respondents Aluminum Company of America, a corporation, and Alcoa Building Products, Inc., a corporation, their successors and assigns, and respondents' officers, agents, representatives and employees (hereinafter "respondents"), directly or through any corporation, subsidiary, division or other device shall forthwith cease and desist from disseminating, causing to be disseminated, paying in whole or in part for, or supplying information used in developing any advertisements in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, which make any fuel reduction, heat loss reduction, energy savings, fuel savings, or thermal insulation representations for residential aluminum siding whether "insulated" or not.

In advertisements which merely describe respondents' products without any special emphasis on insulated aluminum siding, the term "insulated aluminum siding" may be used to describe aluminum siding which has insulating material added to it during the manufacturing or installing process so long as a specific R-value for the insulating material so added is disclosed in conjunction with the term "insulated aluminum siding."

It is further ordered, That respondents deliver a copy of this order to all present and future personnel or agents of respondents responsible for the design or creation of advertising materials promoting Alcoa residential aluminum siding.

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It is further ordered, That respondents notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondents, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of the order.

It is further ordered, That respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form within which they have complied with this order.

In the Matter of

GENERAL MILLS FUN GROUP, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2965. Complaint, May 15, 1979 — Decision, May 15, 1979

This consent order, among other things, requires a Minneapolis, Minn. subsidiary of General Mills, Inc. in the advertising and sale of its toy products, to cease misrepresenting or failing to make relevant disclosures regarding the performance, operation, use, size or appearance of such products through visual portrayals, descriptions, or commercial production techniques. General Mills, Inc. is also bound by the terms of the order.

Appearances

For the Commission: *Louise R. Jung, John G. Siracusa* and *Robert S. Blacher.*

For the respondent: *Robert J. Fulgency,* Minneapolis, Minn.

Complaint

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that General Mills Fun Group, Inc., a corporation, hereinafter referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

Paragraph 1. Respondent General Mills Fun Group, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Nevada, and with an office and place of business located at 9200 Wayzata Boulevard, Minneapolis, Minnesota.

Respondent General Mills Fun Group, Inc. is a wholly-owned subsidiary of General Mills, Inc. and is comprised of several divisions, including, among others, Kenner Products.

Par. 2. Respondent is now, and for all times relevant to this complaint has been engaged in the production, distribution and sale of a variety of toy products, including, but not limited to, the following Kenner toy products: "Nugget," "Lightnin' TTP," "TTP Trouble Patrol."

Par. 3. Respondent has caused to be prepared and placed for publication and has caused the dissemination of advertising material, including, but not limited to, the advertising referred to herein, to promote the sale of "Nugget," "Lightnin' TTP," and "TTP Trouble Patrol."

PAR. 4. In the course and conduct of its aforesaid business, respondent has caused "Nugget," "Lightnin' TTP" and "TTP Trouble Patrol" in their packages to be transported from its place of business to purchasers thereof located in various other States of the United States and in the District of Columbia. Respondent maintains, and at all times mentioned herein has maintained, a substantial course of trade in said products in or affecting commerce.

PAR. 5. In the course and conduct of its aforesaid business, respondent has disseminated, and caused the dissemination of, certain television advertisements concerning said products in or affecting commerce which were broadcast by television stations located in various States of the United States, and in the District of Columbia, having sufficient power to carry such broadcasts across state lines, for the purpose of inducing the sale of said products in or affecting commerce.

PAR. 6. Typical and illustrative of the statements and representations in respondent's advertisements disseminated by means of television, but not all inclusive thereof, are the following advertisements, attached hereto and made a part hereof as Exhibits A, B and C, respectively: "Dusty-Nugget," "Lightnin' TTP" and "TTP Trouble Patrol."

PAR. 7. Through the use of the aforesaid advertisements, respondent has represented, directly or by implication:

1. That "Nugget" will stand without any human assistance or mechanical aid (see Exhibit A);

2. That a child can exercise a high degree of control over the speed and direction of the "Lightnin' TTP" car when it is launched from the "Lightnin' TTP" launcher and thereby can perform certain acts or series of acts with the "Lightnin' TTP" car as depicted in one of the aforesaid advertisements (see Exhibit B); and,

3. That a child can exercise a high degree of control over the speed and direction of the "TTP Trouble Patrol" motorcycle and car when they are launched from the "TTP Trouble Patrol" launcher and thereby can perform certain acts or series of acts as depicted in one of the aforesaid advertisements (see Exhibit C).

PAR. 8. In truth and in fact:

1. "Nugget" cannot stand without human assistance or mechanical aid;

2. A child cannot exercise a high degree of control over the speed

and direction of the "Lightnin' TTP" car when it is launched from the "Lightnin' TTP" launcher and cannot perform certain acts or series of acts with the "Lightnin' TTP" car as depicted in one of the aforesaid advertisements (see Exhibit B); and,

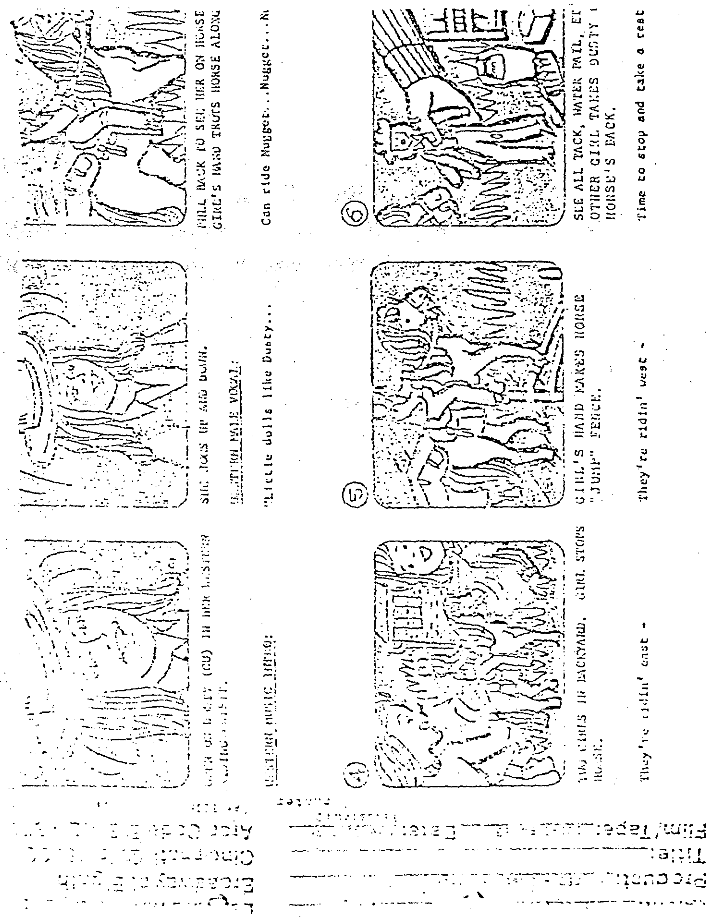
3. A child cannot exercise a high degree of control over the speed and direction of the "TTP Trouble Patrol" motorcycle and car when they are launched from the "TTP Trouble Patrol" launcher and cannot perform certain acts or series of acts as depicted in one of the aforesaid advertisements (see Exhibit C).

Therefore, the statements, representations and depictions referred to in Paragraphs Six and Seven are deceptive and/or unfair.

PAR. 9. The use by respondent of the aforesaid deceptive or unfair advertising has had, and now has, the capacity and tendency to mislead members of the purchasing public into the erroneous and mistaken belief that the said representations were and are true, and into the purchase of substantial quantities of the products of respondent by reason of said erroneous and mistaken belief.

PAR. 10. In the course and conduct of its aforesaid business, and at all times mentioned herein, respondent has been and is now, in substantial competition, in or affecting commerce, with other corporations engaged in the manufacture and sale of toy products.

PAR. 11. The aforesaid acts or practices of respondent, as herein alleged as aforesaid, were and are all to the prejudice and injury of the public and of respondent's competitors, and constituted and now constitute unfair methods of competition in or affecting commerce and unfair or deceptive acts or practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act, as amended.

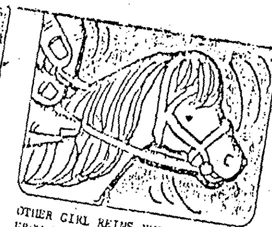

SHE JOGS UP AND DOWN.
WESTERN MALE VOCAL:
"Little dolls like Dusty...
PULL BACK TO SEE HER ON HORSE
GIRL'S HAND TROTS HORSE ALONG
Can ride Nugget...Nugget...N
4
TWO GIRLS IN BACKYARD. GIRL STOPS HORSE.
They're ridin' east -
5
GIRL'S HAND MAKES HORSE "JUMP" FENCE.
They're ridin' west -
6
SEE ALL TACK, WATER PAIL, ET
OTHER GIRL TAKES DUSTY
HORSE'S BACK.
Time to stop and take a rest

Broadway at Eighth
Cincinnati, Ohio 45202
Area Code 513 421-30

Product:
Title:
Film Tape:
Date:

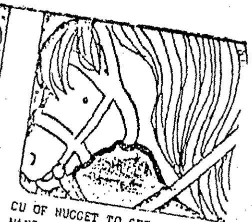
GIRL BRUSHES NUGGET AND GROOMS HER.

GIRL: "Dusty, I just love your riding outfit,



OTHER GIRL REINS NUGGET'S NECK FROM SIDE TO SIDE.

...and your palomino is so beautiful!"



CU OF NUGGET TO SEE HER FLOWI MANE, ETC.

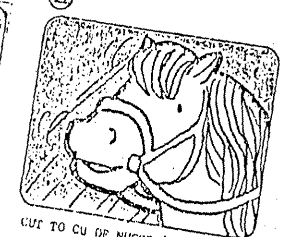
VOCAL: "Silky soft and golden brown -

(10)

GIRL RAISES NUGGET'S HEAD FROM DOWN IN BUCKET.

Time to ride back into town,

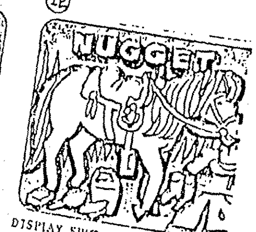
(11)



CUT TO CU OF NUGGET'S HEAD.

On Nugget...Nugget...Nugget."

(12)



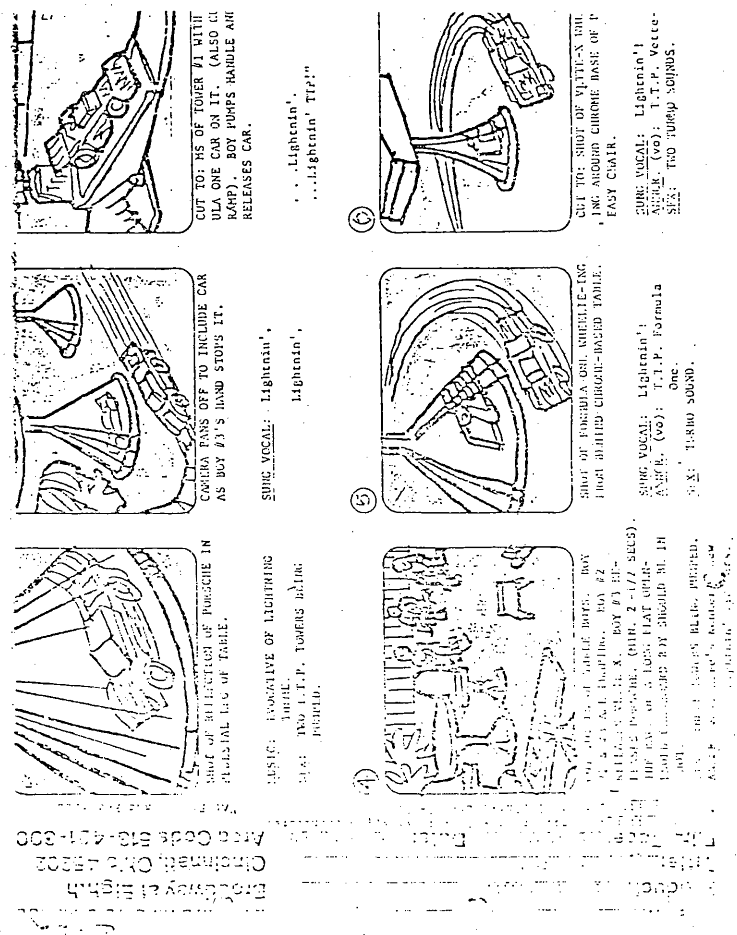
DISPLAY SHOT. ALL ITEMS ON CK BACKGROUND.

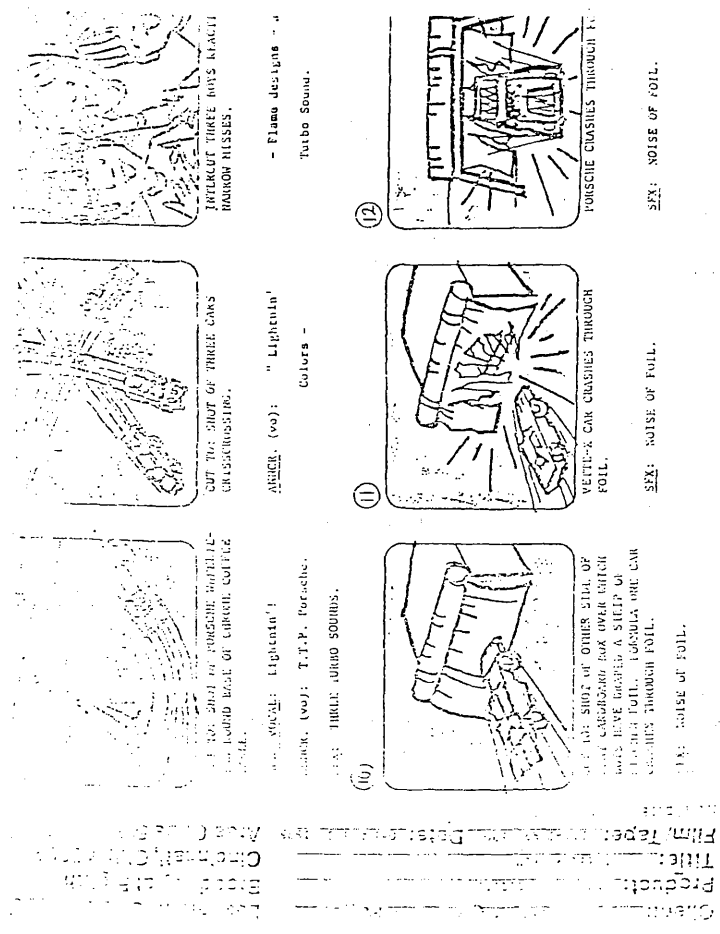
ANNCR: "Nugget, accessories Dusty's riding outfi from Kenner. Bu sold separately!"

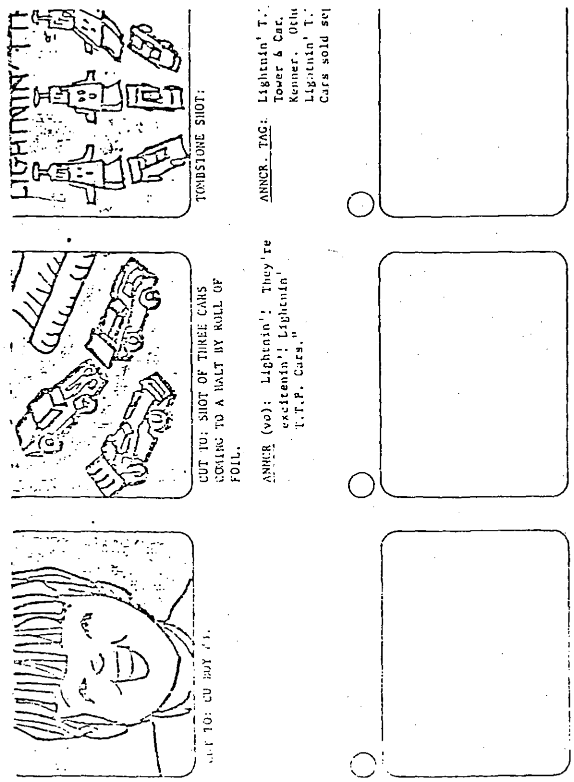
Product: [illegible]
Title: [illegible]
Film/Tape: [illegible] Date: [illegible]

Broadway at Eighth
Cincinnati, Ohio [illegible]
Area Code 513-[illegible]

Video	Audio
[illegible] DUSTY ([illegible] IN HER WESTERN RIDING OUTFIT.	WESTERN MUSIC INTRO:
SHE JIGS UP AND DOWN.	WESTERN MALE VOCAL:
	"Dusty...Dusty...Dusty...
PULL BACK TO SEE HER ON HORSE. GIRL'S HAND TROTS HORSE ALONG.	ridin' Nugget...Nugget...Nugget
TWO GIRLS IN BACKYARD. GIRL STOPS HORSE.	They're ridin' east,
GIRL'S HAND MAKES HORSE "JUMP" FENCE.	They're ridin' west -,
SEE ALL TACK, WATER PAIL, ETC. OTHER GIRL TAKES DUSTY OFF HORSE'S BACK.	Time to stop and take a rest."
GIRL BRUSHES NUGGET AND GROOMS HER.	GIRL: "Dusty, I just love your riding outfit, and your palomino is so beautiful!"
OTHER GIRL REINS NUGGET'S NECK FROM SIDE TO SIDE.	
CU OF NUGGET TO SEE HER FLOWING MANE, ETC.	VOCAL: "Silky soft and golden brown -
GIRL RAISES HORSE'S HEAD FROM DOWN IN THE BUCKET.	Time to ride back into town -
CUT TO CU OF NUGGET'S HEAD.	On Nugget...Nugget...Nugget."
DISPLAY SHOT. ALL ITEMS ON GRASS BKG.	ANNCR: "Nugget, accessories, and Dusty' ridin' outfit, from Kenner. -- Dusty sold separately."

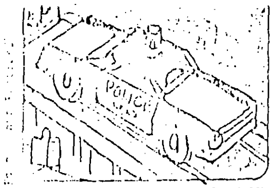

CAMERA PANS OFF TO INCLUDE CAR AS BOY #3'S HAND STOPS IT.
SUNG VOCAL: Lightnin',
Lightnin',
RELEASES CAR.
. . .Lightnin'.
...Lightnin' TTP!"
5
SHOT OF FORMULA ONE WHEELIE-ING FROM BEHIND CHROME-BASED TABLE.
SUNG VOCAL: Lightnin'!
ANNCR. (vo): T.T.P. Formula One.
SFX: TURBO SOUND.
6
EASY CHAIR.
SUNG VOCAL: Lightnin'!
ANNCR. (vo): T.T.P. Vette-
SFX: TWO TURBO SOUNDS.


SHOT OF PORSCHE
VOCAL: Lightnin'!
(vo): T.T.P. Porsche.
THREE TURBO SOUNDS.
CUT TO: SHOT OF THREE CARS CRISSCROSSING.
ANNCR. (vo): " Lightnin' Colors -
INTERCUT THREE BOYS REACTI NARROW MISSES.
- Flame designs -
Turbo Sound.
(10)
SHOT OF OTHER SIDE OF CARDBOARD BOX OVER WHICH
FOIL. FORMULA ONE CAR
THROUGH FOIL.
NOISE OF FOIL.
(11)
VETTE-X CAR CRASHES THROUGH FOIL.
SFX: NOISE OF FOIL.
(12)
PORSCHE CRASHES THROUGH
SFX: NOISE OF FOIL.
Client:
Product:
Title:
Film/Tape:


CUT TO: CU BOY
CUT TO: SHOT OF THREE CARS COMING TO A HALT BY ROLL OF FOIL.
ANNCR (vo): Lightnin'! They're excitenin'! Lightnin' T.T.P. Cars."
LIGHTNIN' T.T.
TOMBSTONE SHOT:
ANNCR. TAG: Lightnin' T. Tower & Car. Kenner. Oth Lightnin' T. Cars sold se

Broadway at Eighth
Cincinnati, Ohio 45202
Area Code 513-421-30

Product: ...
Title: ...
Film/Tape: ... Date: ...

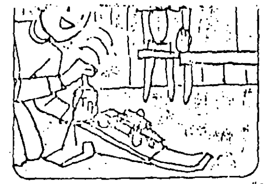


... OF POLICE CAR ON LAUNCH ... OF TTP PUMP.

... OPEN. - :01½ SEC. ROLL UP.

SFX: (TTP PUMP WHINE)

... JOHNNY CASH TYPE JINGLE.



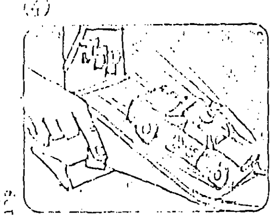
PULL BACK: TO INCLUDE BOY #1 OPERATING PUMP WITH CURVED RAMP SECTION ATTACHED. (BASEMENT PLAYROOM)

SINGER (vo): TTP Trouble Patrol!

CUT TO: BOY #2 FINISH... ASSEMBLING CRASH WALL ARE USING AS "BANK". ... ROBBERS IN IT. ALL I... SHOWN.

SINGER (vo): Things ... happeni... at 6th

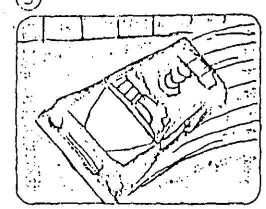
(4)



CU. TO: ... OF POLICE CAR ... BOY RELEASES IT.

SINGER (vo): He gets there quick!

(5)

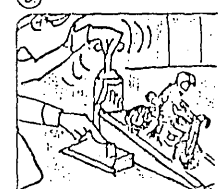


CUT TO: POLICE CAR RACING IN A SEMI-CIRCLE ON TWO WHEELS ACROSS PAVEMENT FLOOR.

SFX: CAR SOUND

SINGER (vo): Wastes no time!
ANNCR (vo): Kenner's ... TTP Troubl...

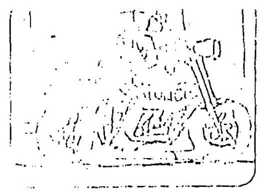
(6)



DISSOLVE TO: BOY #2 ... WITH CYCLE ON RAMP. MAN IS ON CYCLE. BOY RELEASES CYCLE.

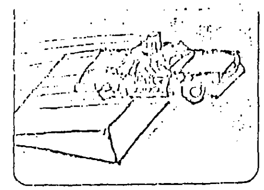
ANNCR (vo): with Police Cl... Team.

SINGER (vo): Car and



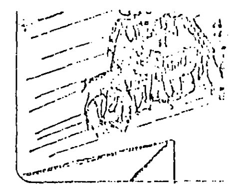
CUT TO: CYCLE RACING ACROSS

SFX: TURBO-SOUND
SINGER (vo): Givin' chase.
Cops 'n robbers,



CUT TO: CAR GOING UP RAMP AND JUMPS OFF.

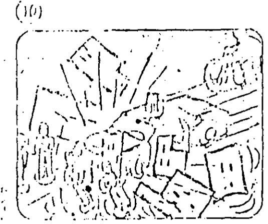
SFX: CYCLE
SINGER (vo): What a race!
Trouble Patrol!
TTP...



CUT TO: CYCLE JUMPING RAMP.

SINGER (vo): That's t
Big 'n to

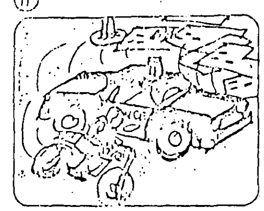
(10)



CUT TO: CAR, CLOSELY FOL- ... BY CYCLE AS THEY BOTH ... "BANK" AND THRU ...

SINGER (vo): You can crash
the car,
Right through
the ...

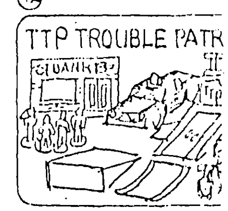
(11)



CUT TO: CU OF POLICE CAR AND CYCLE COMING TO STOP ALONGSIDE THE ROBBERS.

SINGER (vo): Trouble Patrol!
TTP...

(12)



CUT TO: ISLAND SHOT - CAR, CYCLE WITH POLICE SITTING ON IT, 4 ROPS CRASH WALL, JUMP RAMP PUMP WITH CURVED SECT DISPLAYED WITH BOX IN

ANNCR (vo): TTP Trouble
with the Police Chase Tea

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption thereof, and the named respondent having been furnished thereafter with a copy of a draft of complaint which the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the named respondent with violation of the Federal Trade Commission Act; and

The named respondent, General Mills, Inc., and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the named respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by the named respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having considered the matter and having determined that it had reason to believe that the named respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the matter and having determined that it had reason to believe that the named respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, making the following jurisdictional findings, and enters the following order:

1. The named respondent, General Mills Fun Group, Inc., is a corporation organized, existing and doing business under and by virtue of the laws of the State of Nevada, with an office and place of business located at 9200 Wayzata Boulevard, Minneapolis, Minnesota.

2. The named respondent is a wholly-owned subsidiary of General Mills, Inc., a corporation, organized, existing and doing business under and by virtue of the laws of the State of Delaware,

with its office and principal place of business located at 9200 Wayzata Boulevard, Minneapolis, Minnesota.

3. The Federal Trade Commission has jurisdiction of the subject matter in this proceeding and of General Mills Fun Group, Inc. and General Mills, Inc., and the proceeding is in the public interest.

Order

For the purposes of this order:

1. The compression of a television commercial into a short time span shall not be considered a violation of this order so long as it does not result in the misrepresentation to children of the toy's performance or operation.
2. The term "children" shall mean the age group or age groups of children as shown on the packaging for whom the manufacturer recommends use of the toy.
3. The effectiveness of any oral or written disclosure, disclaimer or qualification of any visual portrayal or oral or written description shall be considered in determining whether the advertisement, as a whole, misrepresents to children the toy's performance, operation, size or appearance.
4. The term "commercial production technique" shall include, but not be limited to, the use in commercial production of prototypes or other non-production or modified versions of a toy, controlled action sequences, mechanical or human assistance to child actors in actuating or manipulating the toy during or prior to commercial production, the use of special camera lenses or film or audio techniques, including video or audio overlays or the like, and the use of splicing or editing techniques.
5. The use of "commercial production techniques" shall not be considered a violation of this order so long as they do not result in the misrepresentation to children of the toy's performance, operation, size or appearance.

I

It is ordered, That General Mills Fun Group, Inc., a corporation, its successors and assigns, and its officers, agents, representatives, employees, directly or through any corporation, subsidiary, division or other device, in connection with the advertising, sale, offering for sale or distribution of toys or related products (hereinafter referred to as "toys"), in or affecting commerce, cease and desist from, directly or indirectly, portraying or describing in an advertisement the performance, operation, use, size, appearance, components or similar characteristic of such toy by or through the use of:

A. Any visual portrayal or oral or written description of the performance or operation of a toy in any manner which cannot be duplicated by children in the ordinary use of such toy.

B. Any use of any commercial production technique that results in any visual portrayal or oral or written description which, in the context of the advertisement as a whole, misrepresents to children a toy's performance, operation, size or appearance.

C. Any visual portrayal or oral or written description of the performance or operation of a toy which fails to disclose to children the need for human or mechanical assistance, when such failure, in the context of the advertisement as a whole, misrepresents to children such toy's performance or operation.

II

It is further ordered, That respondent shall forthwith distribute a copy of this order to each of its operating divisions.

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of this order.

It is further ordered, That the respondent herein shall, within sixty (60) days after service upon it of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

III

It is further ordered, That General Mills, Inc., a corporation, its successors and assigns, and its officers, agents, representatives, employees, directly or through any corporation, subsidiary (other than General Mills Fun Group, Inc.), division or other device, shall be bound by the terms of this order in the event it engages in the advertising of toys, in or affecting commerce, excluding those advertisements for toys not manufactured by or for General Mills, Inc. and those advertisements relating to the use of toys as premiums in connection with the sale of non-toy products.

It is further ordered, That General Mills, Inc., a corporation, shall be liable for any penalties or other legal or equitable relief which arise or could have arisen from any suit based on any alleged violation of this order committed by any subsidiary, division or other device of General Mills, Inc. subject to this order (hereafter "company"), or by their officers, representatives or employees, while such company was owned by General Mills, Inc., if, for any reason, such as sale, dissolution, merger, reorganization, insolvency or termination, the company is not amenable to suit or the execution of full judgment.

294-972 O - 80 - 49

IN THE MATTER OF

KAISER ALUMINUM & CHEMICAL CORPORATION

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF SECTION 5 OF THE FEDERAL TRADE COMMISSION ACT AND SECTION 7 OF THE CLAYTON ACT

Docket 9080. Complaint, April 27, 1976 — Final Order, May 17, 1979*

This order requires, among other things, that an Oakland, Calif. manufacturer of various products divest itself completely, within one year from the effective date of the order, of the Lavino Division of International Minerals & Chemicals Corporation, subject to Commission approval; and refrain, for three years, from hiring any individual employed by the purchaser. The order further prohibits respondent from acquiring any business engaged in manufacturing, distributing, or selling basic refractories, for a period of ten years; and provides for arbitration, should disputes arise between respondent and the acquirer.

Appearances

For the Commission: *Tom D. Smith, Kenneth A. Ross* and *George S. Cary.*

For the respondent: *Robert A. Hammond, III, Gary D. Wilson, James R. Farrand, Stewart A. Block* and *Carol D. Weisman, Wilmer, Cutler & Pickering, Washington, D.C.*

COMPLAINT

The Federal Trade Commission, having reason to believe that Kaiser Aluminum and Chemical Corporation, a corporation subject to the jurisdiction of the Commission, has acquired the two operating basic refractory plants, inventory and related assets of the Lavino division of International Minerals and Chemical Corporation, a corporation, in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and/or Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint charging as follows:

* Amended by the September 8, 1977 order of the Administrative Law Judge, which added two new product markets: "B.O.F. bricks and shapes" and "conventionally bonded basic bricks and shapes."

I. Definitions

1. For the purpose of this complaint the following definitions shall apply:

(a) Basic refractories are non-metallic insulating materials composed predominately of magnesia, magnesite, dolomite, chromite, or chrome ore, or a combination thereof.

(b) Basic refractory bricks and shapes are non-metallic insulating materials composed predominately of magnesia, magnesite, dolomite, chromite, or chrome ore, or a combination thereof and which are formed during manufacture into bricks and other special shapes.

(c) Basic refractory specialties are non-metallic insulating materials composed predominately of magnesia, [2] magnesite, dolomite, chromite, or chrome ore, or a combination thereof and which are sold in a "bulk" or non-shaped form.

(d) Basic oxygen furnace (hereinafter "B.O.F.") bricks and shapes are basic refractory bricks and shapes which are bonded or impregnated with coal tar pitch.

(e) Conventionally bonded basic bricks and shapes are basic refractory bricks and shapes which do not contain coal tar pitch and in which mechanical strength is obtained by either a chemical bond or a ceramic bond without an intervening liquid phase.

II. Kaiser Aluminum & Chemical Corporation

2. Respondent Kaiser Aluminum and Chemical Corporation (hereinafter "Kaiser") is now and was at the time of the acquisition hereinafter described a Delaware corporation with its principal office and place of business at 300 Lakeside Drive, Oakland, California.

3. Kaiser is a fully-integrated aluminum producer and a highly-diversified industrial corporation engaged in a number of enterprises including, but not limited to, the production of agricultural chemicals, industrial chemicals, refractories materials and strontium products. In addition, Kaiser is engaged in commodities trading and owns fifty percent of Kaiser Aetna, a large real estate development firm. Kaiser also is engaged in mining or manufacturing in more than a dozen other countries. Kaiser Steel Corporation, an affiliated corporation of Kaiser, is a major consumer of basic refractories and is supplied primarily by Kaiser.

4. In 1973, Kaiser and its subsidiaries had total sales and revenues of $1.28 billion, net income before extraordinary items of $66.54 million, and total assets of $1.81 billion. Kaiser was ranked by

Fortune magazine as the 133rd largest in sales and 67th largest in assets in 1973 among the nation's industrial corporations.

5. Kaiser, prior to the acquisition, operated seven refractory plants in the United States and, in whole or in part, owned six additional plants located in as many other countries.

6. Prior to and since the acquisition Kaiser has been a leading domestic supplier of refractories to the steel, cement and glass industries. [3]

7. In 1973, Kaiser had total domestic refractory shipments of $65.8 million, representing 8.4% of the total United States shipments of refractory products.

8. In 1973, Kaiser had total domestic basic refractory sales of $38.5 million, representing 15.7% of the total United States sales of basic refractory products and ranked number two among the nation's basic refractory producers.

9. In 1973, Kaiser had total domestic basic refractory bricks and shapes sales of $21.4 million, representing 12.2% of the total United States basic refractory bricks and shapes sales and ranked number five among the nation's basic refractory bricks and shapes producers.

10. In 1973, Kaiser had total basic refractory specialties sales of $17.1 million, representing 24.4% of the total United States basic refractory specialties sales and ranked number one among the nation's basic refractory specialties producers.

11. In 1973, Kaiser had total domestic sales of B.O.F. bricks and shapes of $1.75 million, representing 3.9% of the total United States B.O.F. refractories sales and ranked sixth among the nation's B.O.F. bricks and shapes producers.

12. In 1973 Kaiser had total domestic sales of conventionally bonded basic bricks and shapes of $18.5 million, representing 14.02% of the total United States conventionally bonded basic bricks and shapes sales and ranked number five among the nation's conventionally bonded basic bricks and shapes producers.

13. At all times relevant herein, Kaiser sold and shipped the relevant products throughout the United States and was and is now engaged in commerce as "commerce" is defined in the amended Clayton Act and in the amended Federal Trade Commission Act.

III. The Acquisition

14. On February 28, 1974, Kaiser, at a cost of $16.9 million, acquired two basic refractory plants and related assets located at Plymouth Meeting, Pennsylvania and Gary, Indiana. These facilities comprised the Lavino Division of International Minerals and Chemical Corporation (hereinafter "Lavino"). [4]

IV. Lavino

15. In 1973, Lavino had refractory shipments of $27.7 million representing 3.7% of the total United States shipments of refractory products.

16. In 1973, Lavino had basic refractory sales of $27.7 million representing 11.3% of the total United States basic refractories sales and ranked number three among the nation's basic refractory producers.

17. In 1973, Lavino had basic refractory bricks and shapes sales of $25.5 million representing 14.5% of the total United States bricks and shapes sales and ranked number two among the nation's basic refractory bricks and shapes producers.

18. In 1973, Lavino had basic refractory specialties sales of $2.2 million representing 3.1% of the total United States basic refractory specialties sales and ranked number five among the nation's basic refractory specialties producers.

19. In 1973, Lavino had B.O.F. refractory bricks and shapes domestic sales of $3.56 million, representing 7.9% of the total United States B.O.F. bricks and shapes sales, and ranked fourth among the nation's B.O.F. bricks and shapes producers.

20. In 1973 Lavino had total domestic sales of conventionally bonded basic bricks and shapes of $20 million, representing 15.14% of the total United States conventionally bonded basic bricks and shapes sales and ranked number three among the nation's conventionally bonded basic bricks and shapes producers.

21. At all times relevant herein Lavino sold and shipped the relevant products throughout the United States and was engaged in commerce as "commerce" is defined in the amended Clayton Act and in the amended Federal Trade Commission Act.

V. Trade and Commerce

22. The relevant geographic market is the United States as a whole.

23. The relevant product market is the manufacture and sale of basic refractories. The relevant product submarkets are: [5]

(a) manufacture and sale of basic refractory bricks and shapes;

(b) manufacture and sale of basic refractory specialties;

(c) manufacture and sale of B.O.F. bricks and shapes; and

(d) manufacture and sale of conventionally bonded basic bricks and shapes.

A. Basic Refractories Market

24. Trade and commerce in the sale of basic refractories in the United States is substantial, with 1973 sales amounting to $245.8 million.

25. In 1973, prior to the acquisition, concentration in the manufacture and sale of basic refractories was high with the top four firms accounting for 57% of sales and the top eight accounting for 86%.

26. By virtue of the acquisition of Lavino, Kaiser controlled facilities which accounted for 26.9% of the 1973 sales of basic refractories and became *pro forma* the leading manufacturer of basic refractories in that year.

27. On a *pro forma* basis the acquisition of Lavino by Kaiser increased the 1973 four-firm concentration from 57% to 66% and eight-firm concentration from 86% to 90% in sales of basic refractories.

28. There have been no new entrants into the manufacture and sale of basic refractories since 1962.

29. Barriers to entry into the manufacture and sale of basic refractories are high and are increasing.

B. Basic Refractory Bricks and Shapes

30. Trade and commerce in the sale of basic refractory bricks and shapes in the United States is substantial, with 1973 sales amounting to $175.7 million.

31. In 1973, prior to the acquisition, concentration in the manufacture and sale of basic refractory bricks and shapes was high with the top four firms accounting for 66% of sales and the top eight accounting for 94%. [**6**]

32. By virtue of the acquisition of Lavino, Kaiser controlled facilities which accounted for 26.7% of the 1973 sales of basic refractory bricks and shapes and became pro forma the leading manufacturer of basic refractory bricks and shapes in that year.

33. On a pro forma basis the acquisition of Lavino by Kaiser increased the 1973 four-firm concentration from 66% to 79% and eight-firm concentration from 94% to 96% in sales of basic refractory bricks and shapes.

34. There have been no new entrants into the manufacture and sale of basic refractory bricks and shapes since 1962.

35. Barriers to entry into the manufacture and sale of basic refractory bricks and shapes are high and are increasing.

C. Basic Refractory Specialties

36. Trade and commerce in the sale of basic refractory specialties in the United States is substantial, with 1973 sales amounting to $70.1 million.

37. In 1973, prior to the acquisition, concentration in the manufacture and sale of basic refractory specialties was high with the top four firms accounting for 80% of sales and the top eight accounting for 92%.

38. By virtue of the acquisition of Lavino, Kaiser controlled facilities which accounted for 27.5% of the 1973 sales of basic refractory specialties and strengthened its position as the largest manufacturer of basic refractory specialties in that year.

39. On a pro forma basis the acquisition of Lavino by Kaiser increased the 1973 four-firm concentration from 80% to 83% and eight-firm concentration from 92% to 94% in sales of basic refractory specialties.

40. There have been no new entrants into the manufacture and sale of basic refractory specialties since 1962.

41. Barriers to entry into the manufacture and sale of basic refractory specialties are high and are increasing. [7]

D. B.O.F. Bricks and Shapes

42. Trade and commerce in the sale of B.O.F. bricks and shapes is substantial, with 1973 sales amounting to $45.1 million.

43. In 1973, prior to the acquisition, concentration in the manufacture and sale of B.O.F. bricks and shapes was high, with the top four producers accounting for 82.7% of sales, and the top eight accounting for 99.0%.

44. By virtue of the acquisition of Lavino, Kaiser controlled facilities which accounted for 11.9% of the 1973 sales of B.O.F. bricks and shapes.

45. On a pro forma basis, the acquisition of Lavino by Kaiser increased the 1973 four-firm concentration from 82.7% to 86.6% in sales of B.O.F. brick and shapes.

46. There have been no new entrants into the manufacture and sale of basic refractory bricks and shapes since 1962.

47. Barriers to entry into the manufacture and sale of B.O.F. bricks are high and are increasing.

E. Conventionally Bonded Basic Bricks and Shapes

48. Trade and commerce in the sale of conventionally bonded

basic bricks and shapes is substantial, with 1973 sales amounting to $132.5 million.

49. In 1973, prior to the acquisition, concentration in the manufacture and sale of conventionally bonded basic bricks and shapes was high, with the top four producers accounting for 75.44% of sales, and the top eight accounting for 96.96%.

50. By virtue of the acquisition of Lavino, Kaiser controlled facilities which accounted for 29.16% of the 1973 sales of conventionally bonded basic bricks and shapes.

51. On a *pro forma* basis, the acquisition of Lavino by Kaiser increased the 1973 four-firm concentration from 75.44% to 84.86% in sales of conventionally bonded basic bricks and shapes.

52. There have been no new entrants into the manufacture and sale of conventionally bonded basic refractory bricks and shapes since 1962. [8]

53. Barriers to entry into the manufacture and sale of conventionally bonded basic bricks and shapes are high and are increasing.

VI. Effects of The Acquisition

54. The effects of the acquisition set forth in Paragraph 14 may be substantially to lessen competition or tend to create a monopoly in the relevant markets, in violation of Section 7 of the Clayton Act, as amended, and the acquisition constitutes an unfair method of competition and unfair act and practice within the meaning of Section 5 of the Federal Trade Commission Act, as amended, in the following ways among others:

(a) eliminating substantial competition between Kaiser and Lavino and among Kaiser, Lavino and other competitors in the relevant markets;

(b) significantly increasing the already high levels of concentration in the relevant markets;

(c) significantly raising the already high barriers to entry into the relevant markets;

(d) increasing and threatening to still further increase concentration in the relevant markets through additional mergers by other competitors; and

(e) strengthening the position of Kaiser in the relevant markets.

VII. Violations Charged

55. The acquisition set forth in Paragraph 14 constitutes a violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18).

56. The acquisition set forth in Paragraph 14 constitutes a

violation of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

Initial Decision by James P. Timony, Administrative Law Judge

October 12, 1978

Preliminary Statement

Respondent Kaiser Aluminum & Chemical Corporation is charged with a violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), for its acquisition on February 28, 1974, of two refractory plants and related assets of the Lavino Division of International Minerals & Chemical Corporation. [2]

The complaint issued by the Federal Trade Commission in this proceeding is dated April 27, 1976, and alleges that the acquisition may substantially lessen competition or tend to create a monopoly in the markets for the manufacture and sale of "basic refractories," "basic refractory bricks and shapes," and "basic refractory specialties." (Complaint ¶¶ 18, 37.)

In particular, the complaint alleges that the acquisition violated Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act by:

eliminating substantial competition between Kaiser and Lavino and among Kaiser, Lavino and other competitors in the relevant markets;

significantly increasing the already high levels of concentration in the relevant markets;

significantly raising the already high barriers to entry into the relevant markets;

increasing and threatening to still further increase concentration in the relevant markets through additional mergers by other competitors; and

strengthening the position of Kaiser in the relevant markets. (Complaint ¶ 37.)

Respondent filed its Answer on July 15, 1976, admitting in part and denying in part the allegations of the complaint. Respondent denied that its acquisition of the Lavino plants was unlawful, alleging that, *inter alia,* (1) the markets defined in the complaint were not valid markets in which to judge the effects of the acquisition, (2) technological and competitive changes in the refractories consuming and production industries had left Lavino with no competitive viability at the time of the acquisition, and (3) the actual and probable effects of the acquisition were to increase rather than decrease competition in the refractories industry. (Answer pp. 7–15.)

Prehearing conferences were held in Washington, D.C., on July 26, 1976, October 26, 1976, November 3, 1976, May 18, 1977, and September 2, 1977. Extensive discovery was undertaken by both sides. Subpoenas were issued at respondent's request to a number of other refractories producers. Motions to quash those subpoenas were overruled. One subpoena was enforced in federal court. *FTC* v. *Dresser Industries, Inc.*, 1977–1 CCH Trade Cases ¶ 61,400 (D.D.C. 1977). [3]

After complaint counsel's motion dated August 1, 1977, the complaint was amended by adding two new product markets: "B.O.F. bricks and shapes" and "conventionally bonded basic bricks and shapes."

Presentation of complaint counsel's case-in-chief began in Washington, D.C. on December 1, 1977, and concluded on December 20, 1977. Presentation of Kaiser's defense began in Washington, D.C., on January 9, 1978, and continued through January 20, 1978. Additional defense hearings were held in San Francisco, California, from January 31 through February 3, 1978, and in Washington, D.C., on February 21 and March 2, 3, and 10, 1978. Complaint counsel presented a rebuttal witness on April 7, 1978. Stipulations and other exhibits were received thereafter, and the record was formally closed on July 21, 1978.

In total, 30 witnesses testified: 10 for complaint counsel and 20 for respondent. There are 768 exhibits in the record, 275 of which were introduced by complaint counsel and 493 by respondent. These include physical samples of refractory products and documents totalling almost 11,000 pages. In addition, there are over 4,000 pages of hearing transcripts.

The findings of fact include references to supporting evidentiary items in the record. Such references are intended to serve as guides to the testimony and the exhibits supporting the findings of fact. They do not necessarily represent complete summaries of the evidence supporting each finding. The following abbreviations have been used:

Tr. – Transcript, preceded by the name of the witness and followed by the page number;
CX – Complaint counsel's exhibit, followed by its number and the referenced page(s);
RX – Respondent's exhibit, followed by its number and the referenced page(s);
CPF – Complaint counsel's proposed finding;
RPF – Respondent's proposed finding;

AC - Amended Complaint; and
A - Respondent's Answer to the Amended Complaint. [4]

Definitions

For the purpose of these findings, the following definitions shall apply:

(a) Basic refractories are non-metallic insulating materials composed predominately of magnesia, dolomite or chrome ore, or a combination thereof. (Lowe, Tr. 68–69; Williams, Tr. 95, 97; Sack, Tr. 372; Rook, Tr. 543; RX 66B–F; RX 178M.)

(b) Basic refractory bricks and shapes are non-metallic insulating materials composed predominately of magnesia, dolomite, chrome ore, or a combination thereof and which are formed during manufacture into bricks and other special shapes. (Williams, Tr. 100; Sack, Tr. 373; Lawrence, Tr. 645.)

(c) Basic refractory specialties are non-metallic insulating materials composed predominately of magnesia, dolomite or chrome ore, or a combination thereof and which are sold in a "bulk" or non-shaped form. (Williams, Tr. 100; Sack, Tr. 375; Rook, Tr. 543–45; Lawrence, Tr. 641–42; Hummer, Tr. 756.)

(d) Basic oxygen furnace (hereinafter "BOF") bricks and shapes are basic refractory bricks and shapes which are bonded or impregnated with coal tar pitch. (Williams, Tr. 98; Sack, Tr. 374; Garber, Tr. 863; Lawrence, Tr. 873; Hummer, Tr. 755; Kappmeyer, Tr. 1294; Caito, Tr. 1657; CX 111G–H.)

(e) Conventionally bonded basic bricks and shapes are basic refractory bricks and shapes which do not contain coal tar pitch and in which mechanical strength is obtained by either a chemical bond or a ceramic bond without an intervening liquid phase. (Findings 183–185.) [5]

Findings of Fact

Introduction

A. Refractories

1. Refractories are materials that retain their physical shape and chemical identity when subjected to varying conditions of stress including rapid changes in temperature, physical impact, abrasion, pressure and chemical attack by hot gases or molten materials. (Williams, Tr. 95; RX 61"O"; RX 66B; RX 179E; RX 182M; CX 178L.)

2. Refractories are made from magnesia, chrome ore, dolomite, alumina, fireclay,[1] and silica. (Sack, Tr. 372; RX 66B–F; RX 178M; RX 179G; RX 182M.)

3. Refractories are classified as basic or acid (nonbasic) depending on the inherent chemical reactivity of the raw materials involved. (CX 178L; CX 179G; RX 61L; RX 66B.)

4. Refractories are produced in two general forms: "bricks and shapes" (hereinafter bricks) and "specialties." (Williams, Tr. 100; Sack, Tr. 375; CX 179G; RX 61L.)

5. The bricks range in sizes and configurations. They are commonly measured in terms of standard 9-inch equivalents. (CX 178Z14; RX 61L.)

6. Specialties are unformed compositions which come in lump, ground, powder or paste form. (Rook, Tr. 544–45; Lawrence, Tr. 642; Hummer, Tr. 756; Garber, Tr. 860; RX 61L–M; CX 179G.)

B. Preparation of Refractories

7. Preparation of refractories varies from little more than just mining and combining raw materials to complex grinding, screening, molding and firing procedures. (CX 178Z13; CX 179I; RX 66F–K.)

8. The first step in the production of refractories is to remove the impurities and fluxes from the raw materials. Next the raw materials are crushed, ground, screened and mixed. These operations vary depending upon the density, porosity, strength, spalling resistance and thermal characteristics desired in the finished refractory. (CX 178Z13; CX 179I–N; RX 66F.) [6]

9. At this stage the refractories are "specialties." If bricks are to be made, the raw materials, combined with appropriate "binders," are molded and dried. Most bricks are then fired.[2] Those which are not fired, known as chemically bonded bricks, are ready for packaging and shipping. (CX 179N–O.)

10. Firing of bricks, performed either in batch or tunnel kilns,[3] causes a ceramic bond that provides the brick with high temperature strength. The nature of the bond depends on the kind of raw materials and binders and on the temperature at which the brick is fired. (Williams, Tr. 146–47; Caito, Tr. 1596–97; CX 179–O; RX 66K.)

11. After firing and cooling, some bricks are packaged and

[1] "Fireclay" is a nonbasic refractory containing less than 50% alumina. Nonbasic refractories containing more than 50% alumina are called "high alumina." (Williams, Tr. 95–96; Garber, Tr. 858.) Glossaries of industry terms are found at CX 95Z280; CX 205Z203; CX 232Z.

[2] "Fired" means cooked in a kiln at 2700 degrees Fahrenheit and up. (Lawrence, Tr. 660.)

[3] In a "batch kiln" the kiln is raised off the floor, cars with the raw materials are pushed on a track under the kiln, the kiln is lowered and the firing takes place. In a "tunnel kiln" the cars roll through the kiln without the kiln being raised. (Williams, Tr. 118–19.)

shipped. (Williams, Tr. 104; Sack, Tr. 380; CX 179-O.) Other bricks are encased in thin plates of steel (known as cladding) (Williams, Tr. 104; Sack, Tr. 379), or are internally plated with steel. (Garber, Tr. 982.) Some bricks which have been fired are subsequently impregnated with tar. (Williams, Tr. 98; Sack, Tr. 381–82; Garber, Tr. 863.)

C. Refractory Uses

12. Refractories are used whenever it is necessary to confine or control high temperatures. They are used in a wide variety of applications from home fireplaces to nose cones of space capsules to various industrial applications. (CX 178G; CX 179E; RX 61"O".)

13. The industrial applications for refractories include steel furnaces, copper smelters, aluminum furnaces, cement kilns, glass melters, reactors in petroleum refineries, power generators and mineral processing equipment. (CX 178N; CX 179E; CX 182M; RX 61"O"–Z16.)

14. At least 80 percent of all basic refractories, on a dollar or equivalent basis, is sold to the steel industry. (Williams, Tr. 122; Sack, Tr. 388, 486; Rook, Tr. 574; Lawrence, Tr. 673; Hummer, Tr. 841; Garber, Tr. 878–81; Kappmeyer, Tr. 1269–70; Burriss, Tr. 1432; CX 20N; CX 111I; RX 60; RX 62D.) [7]

15. About 95 percent of all basic refractories purchased by the steel industry is used in open hearth furnaces (OHF), electric arc furnaces (EAF) and basic oxygen furnaces (BOF) (Garber, Tr. 880; Gaydos, Tr. 1194; Kappmeyer, Tr. 1268–70), in which iron is converted to steel and in argon oxygen decarburization (AOD) furnaces in which carbon steel is refined to form stainless steel.[4] (Williams, Tr. 128, 129, 138, 154; CX 178Z21, Z25, Z28, Z30; RX 62H–Q; RX 66.)

16. Basic refractories must be used in the steel-making furnaces and handling equipment where they contact slag. Slag is created in the steel-making furnace when the impurities in the molten metal rise to the top of the bath.[5] (Williams, Tr. 131.) Basic refractories resist the corrosive nature of slag. Nonbasic refractories cannot be used for this purpose. (Sack, Tr. 459–60.)

17. The open hearth furnace, which has decreased in importance in the last decade (CX 178Z26), is a relatively shallow container. A burner at one end of the furnace is fired and hot air and exhaust gases are blown across the bath and through a regenerator chamber

[4] In 1973, the three steel-making furnaces were OHF's, BOF's and EAF's (RX 66Z2.) The AOD came into use in 1976. (Hummer, Tr. 768.)

[5] The "bath" in a steel-making furnace refers to the puddle of liquid after the charge is heated and melts. (Williams, Tr. 131.)

at the other end of the furnace, heating the refractory bricks located there. The airflow is periodically reversed and the burners on the opposite end are fired. (Sack, Tr. 388; CX 178Z25; RX 61U.) In some OHF's, pipes are inserted in the roof through which oxygen is blown into the furnace to increase the temperature and to speed the chemical reactions. (Williams, Tr. 129.)

18. OHF's require large quantities of refractories for initial construction, substantial maintenance materials in the course of operation and a major rebuilding about every six months. (CX 178Z28; RX 61U.)

19. OHF's produce as much as 500 tons of steel per heat[6] and each heat takes six to twelve hours. (RX 61U.) OHF's use about ten pounds of basic refractories per ton of steel produced. (RX 132I.) [8]

20. Electric arc furnaces usually produce steel from a cold charge of scrap metal, rather than from molten iron. EAF's are relatively deeper containers than OHF's and have roofs through which extend large electrodes. (Williams, Tr. 128; Kappmeyer, Tr. 1258; CX 178Z30; CX 180Z.)

21. EAF roofs and linings require refractory rebuilding every 10 to 60 days and EAF bottoms require rebuilding about once a year. (RX 61X)

22. EAF's produce about 350 tons of steel per heat and each heat takes three to five hours. (CX 180Z; RX 60-O.) EAF's use about ten pounds of basic refractories per ton of steel produced. (RX 132I-J.)

23. The basic oxygen furnace, a deeper container than OHF's or EAF's, which has no roof, has emerged as the primary steel-making furnace. (CX 178Z29.) Oxygen is blown from the top (or from the bottom in Q-BOP's—Kappmeyer, Tr. 1254) at very high velocities to remove the carbon from the iron and to form steel. (Williams, Tr. 138-39; Kappmeyer, Tr. 1251-53; CX 178Z29; RX 61U.)

24. BOF's produce about 100 to 300 tons of steel per heat and each heat takes about an hour. (CX 178Z28-Z30; RX 61U-X.) BOF's use four to seven pounds of basic refractories per ton of steel produced. (RX 132I; RX 249; RPF 64.)

25. Argon oxygen decarburization furnaces further remove the carbon and other impurities from steel. (Williams, Tr. 154; Sack, Tr. 402-05.)

26. In the early 1960's, most domestic steel was produced by OHF's. However, by 1969, BOF's were producing as much steel as OHF's; and by 1971, BOF's accounted for one-half of all domestic steel production. Today, BOF's produce two-thirds of all domestic

[6] A "heat" is the "cycle of charging raw material to the furnace and discharging finished steel." (Williams, Tr. 135.)

steel. This technological development in the steel industry has had a major impact on the refractory industry. (Caito, Tr. 1589; RX 6A; RX 495—Herbst 41.)

27. BOF's do not use the same types of bricks used in OHF's because the temperature and turbulent activity in BOF's create severe conditions. (Caito, Tr. 1589; RX 60K; RX 61U.) [9]

28. OHF's, BOF's, EAF's and AOD's use a variety of types of basic refractories, although some types are suitable only for one furnace or for part of one furnace. (CX 178Z28-Z30.)

29. The types of refractories used in a furnace in large part depend upon how a furnace is zoned. All furnaces are zoned. Zoning is a process in which the furnace is built with various types of refractories in different patterns so that the entire furnace lining wears out at the same time. (Williams, Tr. 127; Sack, Tr. 390, 394, 400, 404; Garber Tr. 886.) It is customary to put a cheaper refractory in the low wear areas and the best refractory in the high wear areas. (Williams, Tr. 127; Sack, Tr. 390; Garber, Tr. 886; Gaydos, Tr. 1189; Kappmeyer, Tr. 1273.)

30. Zoning practices vary from plant to plant and from furnace relining to relining. (Williams, Tr. 127; Gaydos, Tr. 1189, 1193; Kappmeyer, Tr. 1281, 1290; Mittsoff, Tr. 1766; Ackerman, Tr. 1876-77.) Zoning decisions are based on the quality of steel produced (Garber, Tr. 1121; Kappmeyer, Tr. 1281; Ackerman, Tr. 1877), the size of the ingot manufactured (Gaydos, Tr. 1189), the source of scrap steel utilized (Garber, Tr. 1121; Gaydos, Tr. 1189; Ackerman, Tr. 1877) and the level of steel production (Williams, Tr. 128; Ackerman, Tr. 1877).

31. The quality of refractories is of critical importance in the steel industry. (Lawrence, Tr. 719; Garber, Tr. 1058-60; RX 60B.) The steel companies aim for the lowest possible refractory cost per ton of steel produced. (Garber, Tr. 1058-61.) Refractories producers meet with their steel customers to discuss production problems and research and development suggestions. (Lawrence, Tr. 721; Garber, Tr. 1060; Kappmeyer, Tr. 1399-1401.) Refractories producers also provide technical personnel to assist steel companies in selecting and installing refractories. (Garber, Tr. 1062.)

Respondent Kaiser

32. Respondent Kaiser Aluminum & Chemical Corporation is, and was at the time of the acquisition, a Delaware Corporation with its principal office and place of business at 300 Lakeside Drive, Oakland, California. (AC&A¶ 2.) [10]

33. Kaiser is a fully integrated aluminum producer and a highly

diversified industrial corporation engaged in a number of enterprises, including the production of agricultural chemicals, industrial chemicals and refractories materials. In addition, Kaiser is engaged in commodities trading and mining or manufacturing in more than a dozen countries. (AC&A ¶ 3.)

34. In 1973, Kaiser and its subsidiaries had total sales and revenues of $1.28 billion, net income before extraordinary items of $44.54 million and total assets of $1.81 billion. Kaiser was ranked by *Fortune* magazine as the 133rd largest in sales and 67th largest in assets among the nation's industrial corporations. (AC&A ¶ 4; CX 93V.)

35. Kaiser Refractories, a division of respondent Kaiser, manufactures and markets a broad line of refractory products. (CX 13E.)

36. Kaiser supplies refractory products to the iron and steel, glass, cement, petroleum, chemical and copper industries. (Knight, Tr. 2394; CX 13E-G.)

37. In addition to its United States refractories plants and sales offices, Kaiser has a refractories subsidiary in Oakville, Ontario, Canada; and owns interests in companies which manufacture and sell refractories in South America, Europe and Australia. (CX 95P.)

38. Kaiser began producing basic refractories in 1943 at Milpitas, California, (Knight, Tr. 2375) and later added plants at Natividad and Moss Landing, California. (Knight, Tr. 2377-78.)

39. During the 1950's, Kaiser became well established as a supplier of basic specialties to steel producers. (Knight, Tr. 2373, 2380.)

40. In 1956, Kaiser built a basic refractories plant at Columbiana, Ohio (Knight, Tr. 2381; CX 12Z-15; CX 88B; RX 68L), to enable Kaiser to expand its sales to the major steel producers. (Knight, Tr. 2382-83.)

41. In 1959, Kaiser acquired the Mexico Refractories Company of Mexico, Missouri. (Knight, Tr. 2383-84; CX 12Z16; RX 68G.) Mexico Refractories produced nonbasic refractories, including silica bricks and clay and alumina bricks and specialties at facilities located in Van Dyke, Pennsylvania; Niles, Ohio; Mexico, Missouri; and Frostburg, Maryland. (Knight, Tr. 2383; RX 63G.) In 1965, Kaiser bought Denver Fire Clay's refractories business. (CX 13Z11.) [11]

42. In the mid 1960's, in order to enlarge its capacity for producing basic bricks, Kaiser constructed high temperature tunnel kilns at Moss Landing and at Columbiana. (Knight, Tr. 2384-85; CX 12Z28.)

43. By 1970, Kaiser needed additional high temperature kiln capacity to produce higher performance basic bricks. (Knight, Tr.

2388-89; Adams, Tr. 2465-66, 2468, 2499; CX 100I.) Mr. Knight, a Kaiser vice-president, contacted International Minerals & Chemical Corporation (IMC) to see if they might be interested in selling the Lavino plant at Newark, California. (Knight, Tr. 2390.) IMC declined, and Kaiser started a new kiln at Moss Landing. (Knight, Tr. 2390.) When the new kiln at Moss Landing was half completed, IMC contacted Mr. Knight to inquire whether Kaiser was still interested in the Newark plant. (Knight, Tr. 2390.) Kaiser declined, and the Lavino machinery at Newark was auctioned and its high temperature kiln was bulldozed. (Knight, Tr. 2390.)

44. In the late 1960's, Kaiser's Columbiana plant began producing BOF bricks. (Knight, Tr. 2391; Van Dreser, Tr. 2744-45.) In 1973, Kaiser sold $1.6 million of tar bonded bricks. (Adams, Tr. 2569-70; Neely, Tr. 2807; CX 138D, *in camera.*)

45. By 1973, Kaiser was a vigorous and successful competitor in the sale of basic refractories to the steel, cement, glass and copper industries. (Knight, Tr. 2394.) Kaiser refractories division has historically been one of the most profitable companies in the basic refractories industry and one of the most profitable business segments of Kaiser. (CX 11E-G; CX 46A-C; CX 56Z23, Z32-Z33.)

46. By 1973, Kaiser was considering the possibility of either constructing or acquiring a facility for the production of raw materials used in making basic refractories. (Knight, Tr. 2404-05; Smith, Tr. 2817; CX 56Z4, Z6, Z8.)

47. Kaiser needed increased production capacity in 1973 for high quality basic bricks due to the continuing upgrading of refractories used in the industries served by Kaiser. (Knight, Tr. 2388-89, 2395-96; Adams, Tr. 2464, 2468-69, 2498-99; Van Dreser, Tr. 2760-71; CX 56Z8; CX 100D, *in camera,* I, J, N; RX 74B; RX 76C.) [12]

E. J. Lavino

A. Lavino As an Independent Company

48. E. J. Lavino and Company was founded by Edward J. Lavino in Philadelphia in 1887 and within a few years became a substantial importer of manganese, chrome ore and other mineral ores for sale to the American steel industry. (RX 111A; RX 112I; RX 115G.) World War I created a refractories shortage, and Lavino began making fireclay refractory bricks in a plant at Plymouth Meeting, Pennsylvania, where it had previously made building bricks. (RX 111C; RX 112J; RX 115H; RX 115K; RX 495—Herbst 13-14.)

49. After World War I, Lavino changed from the production of fireclay refractories to the production of basic refractories at the

Plymouth Meeting plant. (RX 111C; RX 115H; RX 495—Herbst 13-14.)

50. In the early 1950's, Lavino constructed a refractories plant at Newark, California, to obtain freight savings in products for the West Coast market. (RX 118Y; RX 495—Herbst 30.)

51. In 1960, Lavino constructed a plant for the production of raw materials used in basic refractories at Freeport, Texas. (Hall, Tr. 2224.)

52. Also in 1960, Lavino constructed a new basic refractories plant at Gary, Indiana, to supply steel producers. (Hall, Tr. 2205; RX 132Z14.)

53. Lavino was an innovative basic refractories producer. In 1962, Lavino produced the first direct bonded basic refractory brick.[7] (Sack, Tr. 525; Hall, Tr. 2222-24.) Lavino was also the first to produce plastic chrome ore (1930); first to manufacture a fosterite bonded chrome/magnesia brick (1932); first to fire chrome and magnesia brick in continuous tunnel kilns (Plymouth Meeting - 1925); first to make chrome refractories for metallurgical furnaces (1920's); first to make refractories from Cuban chrome ore (1920's); first to make refractories from Philippine chrome ore (1940's); [13] first to make refractories from Transvaal chrome ore (1959); first to use sea water periclase[8] for refractories (1938); first to use chemically and physically corrected calcine chrome ore for refractories (Cuban chrome ore processed in Plymouth Meeting - 1929); first to sell chrome refractories to the paper industry (1930's); first to design and construct a shaft kiln for firing high purity periclase at 4,000°F (Freeport - 1960); first to use 98% magnesia for refractories (1960); first to develop the 3" by 3" brick design for open hearth roofs (1959). (Hall, Tr. 2204-05, 2209-17; RX 114T.)

54. In 1963, Lavino added a tar bonding facility to its Gary plant and made its first attempt to get into the BOF refractories business. (Bergey, Tr. 2050; Hall, Tr. 2202-03, 2229-30.)

55. In 1966, Lavino sold to IMC its refractories business for ıpproximately $26 million. (Bergey, Tr. 2040-42.)

B. Lavino under IMC

56. In June of 1970, Dr. Marvin Gillis, a vice president at IMC ho had assumed corporate responsibility for Lavino (Gillis, Tr. ˡ43; Bergey, Tr. 2046), concluded that it would be to IMC's vantage to dispose of Lavino's assets. (Gillis, Tr. 1948-49, 1955-56.)

For definition of "direct bond" basic brick, see Finding 185.

"Periclase" is a high purity magnesia made synthetically by combining dolomite or limestone with sea water, ıitterns or well brines. (Sack, Tr. 549; RX 66C.)

Accordingly, in late 1970, Dr. Gillis discussed with Babcock & Wilcox Co. whether that company might be interested in purchasing Lavino. Babcock & Wilcox determined that it was not interested in Lavino. (RX 224A; RX 225.)

57. In January of 1971, IMC made "changes in [Lavino's] management responsibility." (Bergey, Tr. 2058; RX 495—Herbst 70–71.) Of about 150 Lavino management personnel, IMC terminated 34 officers and employees and transferred 13 others. (Burris, Tr. 1455–60, 1499–1500; Bergey, Tr. 2058–59; RX 127D; RX 495—Herbst 69–71.)

58. This action, as well as statements that IMC wanted to sell its refractories business, damaged the morale of Lavino employees. (Bergey, Tr. 2059; Seelig, Tr. 2130–31.) [14]

59. IMC's overall management philosophy regarding Lavino in the early 1970's was to cut costs. (Kennedy, Tr. 2007–08; Hall, Tr. 2251–53.) Expenditures were limited to those things which were necessary to maintain the day-to-day operations of the business. (Gillis, Tr. 1952–53; Kennedy, Tr. 2008–09.) Pursuant to that policy, IMC tried to cancel the purchase of new presses but was not able to do so. (Hall, Tr. 2245, 2252.) Even after the presses were installed, the money needed for engineering and operational costs were not expended, and two Laeis presses, purchased at a total cost of more than $800,000 to assist Lavino's BOF brick efforts, were never used for commercial brick production. (Hall, Tr. 2246–49; RX 193M.) Similarly, a Bickly kiln, purchased for $300,000, was only used twice because it cost too much to operate. (Hall, Tr. 2249–51; RX 189I.)

60. Cost cutting policies affected Lavino's plant operations. Lavino, which had long been recognized for quality burned and direct bonded brick, began shipping bricks even though they were not in conformity with Lavino's product specifications. (Hall, Tr. 2254–55, 2257–58.) As a result, Lavino's reputation as a quality supplier began to slip, and some steel producers (including Bethlehem, which had long been Lavino's biggest customer) began arranging for alternative suppliers. (Young, Tr. 1796–97; RX 495—Herbst 79–81.)

61. In August 1971, IMC decided to close Lavino's Newark plant (Gillis, Tr. 1960; RX 129A–B; RX 130) contrary to the opinion of Lavino's refractories managers. (Hall, Tr. 2258–59; RX 495—Herbst 68.) The primary ground for their opposition was that closing the plant would weaken Lavino's sales to the copper and cement industries. (Hall, Tr. 2259; RX 495—Herbst 67–69, 101–03.)

62. The largest refractories company in Europe, Didier-Werke A.G., considered purchasing Lavino and in October of 1971, sent five of their personnel to spend two weeks in the United States analyzing

Lavino's business. (Mahler, Tr. 2994-95.) Didier, however, decided that it was not interested in acquiring Lavino even though it found Lavino's products to be a good "top quality." (RX 137H.) Didier found that Lavino's sales force and technical service were undermanned. (RX 137L.) [15]

63. In 1972, IMC closed the Lavino Freeport magnesia plant (Gillis, Tr. 1961-62) and entered into a contract with Harbison-Walker for the purchase of direct bond and tar bond grade magnesia. (RX 362D, *in camera.*) Lavino was forbidden under the contract to use Harbison-Walker grain for tar impregnated brick. (Garber, Tr. 1020-21; RX 362D-E, *in camera.*)

64. The decision to close Freeport was made over the objections of Lavino's refractories management who were concerned that Lavino would be vulnerable to raw materials shortages in periods of high refractories demand. (Garber, Tr. 1032; Hall, Tr. 2260-62, 2326; RX 495—Herbst 68.) To keep Freeport in operation, however, further capital expenditures of about $1 million would have been required to solve air pollution problems. (Gillis, Tr. 1962, 1982.)

65. IMC reduced Lavino's R&D expenditures from $636,000 in fiscal 1971 to $532,000 in fiscal 1972 to $404,000 in fiscal 1973. (CX 125B; CX 127B; RX 190P, RX 190S; RX 192S; RX 194Q.)

66. The R&D cut backs were achieved by reducing expenditures for new equipment and in areas such as Lavino's pilot plant operation for making test quantities of new products including BOF bricks. (Hall, Tr. 2320-21.)

67. The ceramic engineers and other professionals in Lavino's R&D group, who were generally highly regarded in the industry, stayed with the company despite reduced expenditure levels (Hall, Tr. 2300, 2320-21; Van Dreser, Tr. 2655) and despite the fact that they received no pay raises for several years. (Van Dreser, Tr. 2657.)

68. By 1973, Lavino met the tar bonded and tar impregnated brick specifications established by Bethlehem Steel Company, one of the largest users of BOF bricks. (Burriss, Tr. 1471-73; Bergey, Tr. 2066-67; RX 139A; RX 143A; RX 495—Herbst 55.)

69. IMC liquidated the Newark plant in 1972. The machinery and equipment were auctioned off, the building and the direct bond kiln were bulldozed, and the property was sold for non-refractories use. (Gillis, Tr. 1959; Knight, Tr. 2390.) The Freeport plant was similarly dismantled and sold off for other purposes. (Gillis, Tr. 1961.) [16]

70. The refractories industry had a poor financial year in 1971. CX 56P.) In the second half of 1972, the level of steel production ncreased, which led to increased refactories shipments. (RX 193W.) 973 was a record steel production year. (RPF 63.)

71. By the end of 1974, only Lavinosa—a profitable South African chrome mining operation—remained a part of IMC. (RX 195Z3.) Of the 10 Lavino facilities acquired by IMC, five—Newark (refractories), Freeport (magnesia), York (ore grinding), Lynchburg (ferromanganese), and Sheridan (ferromanganese)—had been liquidated. (Burriss, Tr. 1420–21; Bergey, Tr. 2042–43; RX 495—Herbst 145.) Of the other five, Plymouth Meeting and Gary were sold to Kaiser; Eufaula (alumina) was sold to Harbison-Walker; Covington (manganese dioxide) was sold to Ray-O-Vac; and Port Richmond (ore grinding) was sold to Combustion Engineering. (Burriss, Tr. 1420–21; Bergey, Tr. 2042–43; RX 495—Herbst 145–46.)

72. Lavino had divisional earnings of $3,433,000 in fiscal year 1968–69 (RX 186F), $2,873,000 in fiscal year 1969–70 (RX 188F), $17,000 in fiscal year 1970–71 (RX 190D), $2,380,000 in fiscal year 1972–73 (RX 194C), and $1,779,000 in the first half of fiscal year 1973–74 (RX 195B). During the depressed steel producing period, fiscal year 1971–72, Lavino had a divisional loss of $340,000. (RX 192D, G.)

The Lavino Acquisition

73. In the fall of 1972, Kaiser considered acquiring International Minerals & Chemical Corporation (RX 74A; RX 74E) and its Lavino division. (CX 27; RX 74C; RX 77.)

74. Kaiser's initial interest in acquiring the Lavino refractories assets stemmed primarily from its desire to increase its capacity to produce direct bond basic brick. (Knight, Tr. 2395; Adams, Tr. 2468–69; RX 74B; RX 76C–E.) In early 1973, Kaiser was operating near its direct bond capacity; demand for direct bonded basic brick was projected to grow. (Knight, Tr. 2395–96; CX 59B; CX 100G.) [17]

75. In addition to furnishing additional high temperature kiln capacity, purchasing the Lavino plants would provide Kaiser with additional capability to produce tar bonded brick for use in BOF's. (Knight, Tr. 2397–98.) Also, the Plymouth Meeting, Pennsylvania, plant would enable Kaiser to compete more effectively in supplying the eastern steel mills; and the Gary, Indiana, plant would enable Kaiser to compete more effectively in the Chicago, fast-growing BOF market area. (Knight, Tr. 2398.)

76. An August 1973 report, prepared by Kaiser's refractories division, strongly recommended that the acquisition negotiations go forward based upon the predicted profitability of Lavino's plants. (CX 66D, G, L, O.)

77. In September 1973, Kaiser personnel visited Lavino's Plymouth Meeting and Gary facilities. (Adams, Tr. 2478–80; Bowman, Tr.

2920; CX 69A.) They found that the kilns at Plymouth were in excellent condition and, because a third kiln had been converted to a high temperature capability, Lavino had more direct bond capacity than had previously been estimated. (Adams, Tr. 2479–80; Bowman, Tr. 2921; CX 69A, F.) They also found EPA and OSHA problems at the two plants and it was estimated that an additional $1,800,000 would have to be spent to correct them. (Adams, Tr. 2478–79; Bowman, Tr. 2920–21; CX 69C, D.)

78. On November 9, 1973, Kaiser and IMC signed an earnest money agreement providing $200,000 down payment in "earnest money" in exchange for IMC's permitting Kaiser personnel to conduct a detailed inspection of Lavino's facilities and books. (CX 68A; RX 78C; RX 79E; RX 80.) If Kaiser acquired the Lavino plants, $200,000 was to be credited to the purchase price; and if Kaiser notified IMC within 30 days that it did not intend to pursue the acquisition, $100,000 would be returned. (CX 68A; RX 79E–F; RX 80; RX 82B; RX 83A–B; RX 84; RX 86A–D.)

79. Kaiser prepared a "Lavino Division Acquisition Investigation 30-Day Evaluation," dated December 6, 1973. (Adams, Tr. 2481; CX 72A–Z7.) In the report, Kaiser continued to favor the acquisition and recommended that the investigation proceed. (Adams, Tr. 2504–05; CX 72C.) [18]

80. On January 18, 1974, Kaiser notified IMC that it intended "to enter into negotiations towards a definitive agreement of purchase and sale" of the Lavino refractories assets. (RX 98.) IMC and Kaiser signed the purchase agreement on March 5, 1974, with the sale effective February 28, 1974. (Adams, Tr. 2513–14; CX 1A; CX 1Z23.) The assets were acquired for $2 million in cash and approximately $13 million in promissory notes, with Kaiser assuming approximately $2 million of Lavino's current liabilities. (Adams, Tr. 2513–14; CX 77A.)

81. One of the assets Kaiser acquired from IMC was a contract by which Harbison-Walker agreed to supply magnesia. Kaiser would not have purchased the Lavino assets without this contract. (Knight, Tr. 2414.)

82. Also as a result of the acquisition, Kaiser hired the majority of the professionals in Lavino's basic refractories research and development department, including Lavino's Director of R&D, Research Manager and Laboratory Section Manager, and all of Lavino's Research Engineers. Dr. Mikami, Lavino's R&D Director, became Kaiser's R&D Manager of Basic Refractories. Of the five individuals who for the past four years have constituted Kaiser's R&D Basic Refractories Products Development Section, four of them,

including the section head, are former Lavino R&D personnel. (Van Dreser, Tr. 2717-18, 2723-26; CX 84A-B; CX 105A-K.)

83. Kaiser terminated many of the Lavino marketing and sales personnel. (Adams, Tr. 2485-86; CX 66M.) This amounted to a savings of about $900,000 per year. (CX 72U.)

84. At all times relevant herein, Kaiser was engaged in commerce as "commerce" is defined in the amended Clayton Act and in the amended Federal Trade Commission Act. (AC&A ¶ 13.)

85. At all times relevant herein, Lavino was engaged in commerce as "commerce" is defined in the amended Clayton Act and in the amended Federal Trade Commission Act. (AC&A ¶ 21.) **[19]**

Geographic Market

86. In 1973, Kaiser sold basic refractories in 36 states from either its Columbiana, Ohio, plant or its Moss Landing, California, plant. (CX 6B.)

87. In 1973, Lavino sold basic refractories in 32 states from either its Gary, Indiana, plant or its Plymouth Meeting, Pennsylvania, plant. (CX 38A-Q, *in camera;* CX 78A-S; CX 168H-I; CX 115.)

88. In 1973, Lavino and Kaiser sold basic refractories to 100 identical customer facilities in 33 states. (CX 38A-Q, *in camera;* CX 168H-I.) These 33 states accounted for 98 percent of the United States' steel production. (Williams, Tr. 168-69.)

89. Kaiser had general sales offices in California, Missouri and Ohio and district sales offices in 20 states throughout the United States. (CX 95F.)

90. Lavino warehoused basic refractories at its plants at Plymouth Meeting and Gary and at 10 other locations throughout the United States. (CX 22K.)

91. Lavino accounted for 20 percent of all basic refractories sold to the copper industry, even though copper smelters are located primarily in the West. Originally Lavino sold to the copper industry from its Newark, California, plant, but after it was closed it sold from its Gary and Plymouth Meeting plants. (Burriss, Tr. 1519-20.)

92. Kaiser viewed the whole United States as the appropriate market in which to analyze desirability of the Lavino acquisition. (CX 60B; CX 64G-H; CX 66D.)

93. Basic refractories sellers and steel producing companies recognize the whole United States as the market for basic refractories. (Sack, Tr. 420; Rook, Tr. 577, 599; Hummer, Tr. 783; Burriss, Tr. 1444; Caito, Tr. 1662; CX 221F; CX 270B.) **[20]**

Product Markets

A. Basic Refractories

94. Basic refractories are bricks and specialties, made from magnesia, chrome ore or dolomite, which react chemically at high temperatures, as a "base" as different from an "acid." (Williams, Tr. 96; Sack, Tr. 372; CX 111G.) Nonbasic refractories are made from fireclay, silica and alumina. (Williams, Tr. 95–96; Sack, Tr. 373; Lawrence, Tr. 642.)

95. About 90 percent of all refractories used in the steel industry are basic. (Kappmeyer, Tr. 1269.) About 94 percent of the refractories used in steel-making furnaces are basic. The refractories in OHF's are 98 percent basic; in BOF's and Q-Bop's are 100 percent basic; and in EAF's are 85 percent basic. (Sack, Tr. 397; Kappmeyer, Tr. 1270.)

96. Nonbasic refractories are not resistant to the basic slag and the high temperatures in the steel furnaces. (Williams, Tr. 262; Sack, Tr. 374, 459–60; Rook, Tr. 473; Garber, Tr. 939–41; Kappmeyer, Tr. 1272; Van Dreser, Tr. 2683–84.)

97. Basic bricks and basic specialties are used in place of each other or as companion products to control heat, both as initial materials and for maintenance. (Sack, Tr. 392, 395, 401; Rook, Tr. 576; Garber, Tr. 893, 1073; Kappmeyer, Tr. 1293; CX 95Z91; CX 256G.)

98. Steel furnace operators choose among various quantities of basic bricks and basic specialties according to the demand for steel. During times of high demand, they use basic specialties as a repair material, since basic specialties can be applied without shutting down the furnances. (Sack, Tr. 392; Kappmeyer, Tr. 1306–08.) The amount of basic specialties used in a furnace can exceed the amount of basic bricks. The range of use is from 98 percent basic bricks and 2 percent basic specialties to 32 percent basic bricks and 68 percent basic specialties. (Sack, Tr. 392; Garber, Tr. 1073; CX 270S.)

99. Basic bricks and basic specialties may be used separately or together in building furnace hearths. (Sack, Tr. 395; Kappmeyer, Tr. 1293.) [21]

100. Dollar Sales of Domestic Producers With $1 Million Or More In Sales Of Basic Refractories In 1973
(Thousands of Dollars)
(CX 139)

	Total Basic Refractories	*Basic Bricks*	*Basic Specialties*
Harbison-Walker	60,591	54,605	5,986
Kaiser	33,791	20,310	13,481
Basic Inc.	30,147	10,550	19,597
Lavino	26,467	23,614	2,853
General Refractories	25,880	21,547	4,333
Corhart	25,746	25,415	331

North American (NARCO)	22,374	22,250	124
Quigley	14,510	-	14,510
Martin-Marietta	13,375	-	13,375
J. E. Baker (DBCA)	9,267	4,617	4,650
A. P. Green	6,389	5,244	1,145
Marblehead Lime	4,411	-	4,411
Davis Firebrick	3,695	3,695	-
Valley Mineral	2,935	-	2,935
H. K. Porter	2,423	2,423	-
Combustion Engineering	1,009	-	1,009 [22]

101. Nine of the top ten producers of basic bricks also produced basic specialties. These nine producers account for 97 percent of all basic brick production and 60 percent of all basic specialty production. (Finding 100.)

102. Of the ten largest producers of basic specialties, six also produced basic bricks. (Finding 100.)

103. There are production advantages in producing both basic bricks and basic specialties because some of the same equipment is used. (Sack, Tr. 375; Hummer, Tr. 756–57; Garber, Tr. 876; CX 204Z42–Z49.) A basic refractories manufacturer may switch from producing basic bricks to basic specialties on the basis of customer demand. (Williams, Tr. 111–13.)

104. Basic refractories producers do not shift production facilities to nonbasic refractories during times of low demand for basics because of the contamination involved. Switching production facilities between basic and nonbasic refractories, and vice versa, takes months or even years. (Williams, Tr. 337–38; Lawrence, Tr. 671–72; Hummer, Tr. 774–75; Garber, Tr. 927, 934.) Contamination which might arise in the production of basic refractories made from different raw materials can be stopped by cleaning out the production facilities, allowing for a switch to a different basic refractory in a few hours. (Lawrence, Tr. 665–69.)

105. Basic refractories cannot be made on the same production line as nonbasic refractories. (Williams, Tr. 97; Rook, Tr. 584; Hummer, Tr. 775.) A few refractories manufacturers have produced basic bricks and nonbasic bricks at the same location—in different buildings. (Williams, Tr. 208; Sack, Tr. 373; Lawrence, Tr. 650.) But the walls must be air tight because dust from one can contaminate the other, causing deterioration. (Sack, Tr. 350.)

106. Refractories manufacturers, including Kaiser, distinguish between basic and nonbasic refractories in their product brochures (CX 95; CX 205; CX 230; CX 253) and their marketing studies. (CX 49A–E; CX 100; CX 214; CX 219.) Steel producing companies and

refractories manufacturers recognize basic refractories as a separate product market. (Williams, Tr. 96–97; Sack, Tr. 372; Rook, Tr. 544; Lawrence, Tr. 639, 642; Hummer, Tr. 755; Gaydos, Tr. 1177; Kappmeyer, Tr. 1269.) [23]

107. Kaiser recognizes basic refractories and nonbasic refractories as completely separate product lines. (CX 56N.) Kaiser keeps separate financial records (prices, sales, profits) for basic refractories and for nonbasic refractories. (CX 17; CX 18; CX 31; CX 40; CX 41; CX 51D; CX 102; CX 148.)

108. Manufacturers of basic refractories used in the steel industry do not consider the prices of nonbasic refractories in determining the prices of their basic refractories products. (CX 126D.)

109. Kaiser prices its basic refractories without regard to the prices of nonbasic refractories. (CX 32G; CX 56Q.)

110. Refractories companies have separate research and development departments for basic and nonbasic refractories. (Williams, Tr. 182; Sack, Tr. 426–27.)

111. Different sales personnel are used to sell basic and nonbasic refractories because of the need for different background knowledge. Technical sales specialists in the use of basic refractories assist field salesman in the steel industry. (Garber, Tr. 995; Hegeman, Tr. 1708.)

112. In more than 90 percent of all applications of basic refractories, nonbasic refractories cannot be substituted. (Sack, Tr. 528; Rook; Tr. 584; Kappmeyer, Tr. 1317; Burriss, Tr. 1436.)

113. Different persons buy basic refractories and nonbasic refractories in the steel industry. (Sack, Tr. 424–26; Hegeman, Tr. 1709–10; CX 110B.) The melt shop foreman (in charge of the steel-making furnaces) buys basic refractories. Nonbasic refractories are purchased by the person in charge of iron-making (blast furnaces) and steel heat treating and pouring. (Hegeman, Tr. 1710.) Steel companies buy from two to four basic refractories manufacturers at each plant. (CX 110C–D.)

114. Lavino and Kaiser had many identical customers. (CX 110D.) In 1973, twelve steel plants purchased more than $200,000 in basic refractories from both Kaiser and Lavino. (RPF 421.) [24]

B. Basic Specialties

115. Basic specialties are insulating materials made of magnesia, dolomite or chrome ore (Rock, Tr. 544–45; Lawrence, Tr. 642; Hummer, Tr. 756.) These materials are crushed, ground, sized and mixed. They are neither bonded nor shaped. (Williams, Tr. 100, Sack, Tr. 375; Rook, Tr. 544; Lawrence, Tr. 641.) Nearly all basic specialties are used in the steel industry. (RPF 288.)

116. There are a number of types of basic specialties including, *inter alia,* mortars, ramming mixes, gunning mixes, plastics and castables. (Sack, Tr. 375; Rook, Tr. 544; Kappmeyer, Tr. 1303–04; Caito, Tr. 1615–19; RX 61.)

117. Mortars are used to lay bricks in furnaces. They are made in compositions that are similar to the bricks which they are holding. Mortars are used to make a consistent and continuous refractory lining. (RX 61M.)

118. Gunning mixes are generally used as a maintenance material (patch repairs) but also may be used as refractory linings in confined spaces. Gunning mixes are blown into position by air pressure (pneumatic gun) and are sticky enough to stay in place where they are fired. (Sack, Tr. 391; Garber, Tr. 893; Kappmeyer, Tr. 1305; RX 61M.)

119. Castables are predominately dry refractory materials which are mixed on site with water. They are particularly suited to the molding of very specialized shapes and parts at the installation site. They can be used for forming parts of furnace linings including doors and pits. (RX 61M.)

120. Plastics are ready to use refractory materials shaped in slabs or slices which are usually rammed into place. Heat converts the plastic materials to a solid consistency. Plastics are used as a maintenance material as well as used for forming the bottoms, walls and roofs of furnaces. (RX 61M.)

121. Ramming mixes are basic specialties that are rammed into place to create monolitic refractory surfaces. They are mostly used in furnace bottoms. (Sack, Tr. 391; Kappmeyer, Tr. 1309–10; CPF 159.) [25]

122. Different types of specialties are created by varying the raw materials and size of the fractions. Specialties are made by crushing and grinding raw materials, and segregating the raw materials according to fractions of the same size. The fractions are stored in separate bins. The raw material is then fed into mixers with chemical binders. (Williams, Tr. 111–12; Rook, Tr. 573.)

123. There is a trend towards increased use of gunning of basic specialties in BOF's. (Hummer, Tr. 760.)

124. The production of basic specialties is identical to the production of basic bricks up to the pressing stage. (Williams, Tr. 112–13; Lawrence, Tr. 641; Caito, Tr. 1592.) A basic brick manufacturer can therefore sell specialties merely by adding packaging equipment. (Williams, Tr. 112.)

125. Most producers of basic bricks sell basic specialties, however, many producers of basic specialties do not produce basic bricks.

(Caito, Tr. 1650–51; CX 204; RPF 298, 388, 397.) It costs less to produce specialties than bricks because some equipment necessary for the production of bricks such as brick presses, kilns and impregnators are not necessary for the production of specialties. (Hegeman, Tr. 1694.)

126. Most types of basic specialties can be produced at the same plant and many are produced on the same production line. (Williams, Tr. 111; Rook, Tr. 573; Caito, Tr. 1676; CX 159Z1–Z136; CX 204S–Z126.) Some must be kept separate. Plastic chrome ore specialties, for example, are not made at the same facility as magnesia specialties because of contamination problems. Some basic specialties manufacturers use different facilities for producing chrome ore and magnesia specialties (Garber, Tr. 937; Van Dreser, Tr. 2773; Bowman, Tr. 2905), while others use some of the same facilities. (Williams, Tr. 214–15; Lawrence, Tr. 704–05; CX 69; CX 204Z35; CX 204Z82.)

127. Contamination problems preclude specialties manufacturers from producing basic and nonbasic specialties on the same lines. (Williams, Tr. 113, 214–15; Rook, Tr. 563, 584; Lawrence, Tr. 670.) It takes at least six months to convert a basic line to a nonbasic line. (Rook, Tr. 585.) **[26]**

128. Basic specialties have different characteristics and end uses than nonbasic specialties. At least 90 percent of all basic specialties are used in the steel industry in OHF's, BOF's or EAF's. (Williams, Tr. 120, 166–67; Rook, Tr. 574; Lawrence, Tr. 688; Kappmeyer, Tr. 1304.)

129. Basic specialties are used in combination with basic bricks. (Williams, Tr. 166; Sack, Tr. 401; Kappmeyer, Tr. 1306.) Basic specialties are not used in combination with nonbasic bricks. (Williams, Tr. 166; Lawrence Tr. 687; Gaydos, Tr. 1190–91.)

130. Basic specialties and basic bricks are purchased by different persons in the steel industry. Basic specialties are sold to the steel producing superintendent and basic bricks are sold to the masonary superintendent. (Rook, Tr. 578.)

131. Martin-Marietta is the price leader in basic specialties. (Smith, Tr. 2832–33.) Prices of basic specialties remain firm in the face of price competition from sellers of nonbasic specialties. (CX 56Q.)

132. Basic specialties are recognized by steel producing companies and by basic refractories sellers as a separate product market. (Rook, Tr. 544; Kappmeyer, Tr. 1304–11; CX 16; CX 23; CX 49; CX 95Z91; CX 205Z27–Z29; CX 229Z15–Z20.)

133. Kaiser recognizes basic specialties and nonbasic specialties

as completely separate product lines. (CX 56N.) Kaiser keeps separate financial records (prices, sales, profits) for basic specialties and nonbasic specialties (CX 31; CX 41, CX 51D; CX 102) and recognizes basic specialties as one of the major refractories market sectors. (CX 56M; CX 95.)

134. Kaiser and Lavino both produced basic specialties in 1973. (Williams, Tr. 282, 288; Rook, Tr. 591; Kappmeyer, Tr. 1407; Neely, Tr. 2810; CX 95Z91.)

135. Kaiser's largest selling basic specialty in 1973 was Permanente-165, a magnesia ramming and gunning mix, used primarily for construction of hearths of OHF's and EAF's and for maintenance and repair of working linings of steel-making vessels. P-165 has good thermal resistance. (Knight, Tr. 2378-80; Van Dreser, Tr. 2683.) [27]

136. Lavino's largest selling basic specialty was Plastic-KM, a plastic chrome ore mix used almost exclusively in OHF and EAF doors and in non-steel industrial boiler applications. Chrome ore has less capacity to withstand basic slags and has a low melting point but it is highly resistant to spalling. (Williams, Tr. 288; Rook, Tr. 546; Garber, Tr. 1104; Van Dreser, Tr. 2692, 2701-02.) Lavino also sold some magnesia gunning mix. (Caito, Tr. 1628; CX 204Z82.)

C. Basic Bricks

137. The market for basic bricks includes five types: chemically bonded, direct bonded, regular burned, tar bonded and tar impregnated. (CX 30; CX 40; CX 66M; CX 113G-H; CX 213Z7; CX 219; CX 221B.) Basic bricks are made from magnesia and chrome ore, and, to a small extent, from dolomite. (CX 232R.)

138. In 1973, seven of the top ten basic brick manufacturers made all of the five types of basic bricks. (RPF 305; Williams, Tr. 598; Lawrence, Tr. 722; Garber, Tr. 863; CX 204.)

139. The advantages in producing all five types of basic bricks include: (1) shipping economies, (2) research and development economies, and (3) ability by the buyer who uses several basic refractories to line a furnace to place responsibility on one company for any defects. (Sack, Tr. 422-23; Kappmeyer, Tr. 1343; Burriss, Tr. 1448-54; Hall, Tr. 2281; Adams, Tr. 2510-12.)

140. There are few advantages in producing both basic and nonbasic bricks. (Sack, Tr. 423; Hegeman, Tr. 1707-08; Bergey, Tr. 2091; Hall, Tr. 2281; Adams, Tr. 2511-12.)

141. Research and development expertise in the basic brick area is not applicable to nonbasic bricks and vice versa. (Hegeman, Tr. 1707-08; Ackerman, Tr. 1919-20; Bowler, Tr. 2368.)

142. Refractories manufacturers producing both basic and nonba-

sic bricks employ engineers and other personnel who specialize in basic refractory research. (Lawrence, Tr. 654; Garber, Tr. 902; Hegeman, Tr. 1707–08; Van Dreser, Tr. 2714; Neely, Tr. 2779–80.) Such manufacturers also have specialized equipment for basic research. (Sack, Tr. 426–27; Bowler, Tr. 2368.) [28]

143. Nonbasic and basic bricks can be used in place of each other only in a few applications. (Williams, Tr. 263; Sack, Tr. 458–69; Burriss, Tr. 1435–36; see Findings 95, *supra*, and 171 and 199, *infra*.)

144. Contamination problems hinder the production of basic and nonbasic bricks in the same plants. (CX 159Z1–Z136; CX 207A.) Refractory companies which produce basic and nonbasic bricks at the same plant use completely separate production lines or house the lines in separate buildings. (See Findings 104 and 105, *supra*.)

145. The choice of which basic brick to use is made on the basis of a variety of factors, including thermal shock resistance, hot strength, slag resistance, and thermal conductivity. (Van Dreser, Tr. 2681–82; RX 132Z40.)

146. Research and development is critical to the success of a basic brick refractories manufacturer. (Lawrence, Tr. 697; Hummer, Tr. 779; Garber, Tr. 902; Adams, Tr. 2464.)

147. Competition in the basic brick market centers on the development of high quality products. (Williams, Tr. 182; Sack, Tr. 427; Lawrence, Tr. 697; Hummer, Tr. 779; Garber, Tr. 902, 1059; CX 12"O"–Q; CX 125H; CX 207Q; RX 422A.)

148. New basic brick products are generally an improvement upon prior products. (Williams, Tr. 184; Sack, Tr. 427; Lawrence, Tr. 697.) When one refractory company develops a new product the other refractory companies soon follow with their own versions of the "new" product. (Williams, Tr. 195; Van Dreser, Tr. 2677.) Lavino developed the first commercial direct bonded brick in 1962. (Sack, Tr. 428–29; Garber, Tr. 903; Hall, Tr. 2210.) Lavino was soon followed by Harbison-Walker (RX 495—Herbst 120) and eventually by every basic brick producer. (CX 100L.) In 1972, North American introduced a second generation direct bonded brick and Lavino followed shortly thereafter. (CX 125G.) [29]

149. In 1977, American refractories manufacturers started making a carbon bonded magnesia brick commonly referred to as "PMT." This product, copied from a product first used in Japan, is used at the slag line in EAF's. It is 28 percent carbon, compared to 4 percent carbon in a tar bonded brick. (Williams, Tr. 133–35, 185, 235–36; Sack, Tr. 406–08; Lawrence, Tr. 676–77; Garber, Tr. 1147.) It is relatively easy to make. (Williams, Tr. 346.)

150. All major types of basic bricks can be produced in a well-

equipped plant (Sack, Tr. 375–76; Hummer, Tr. 757–58; Garber, Tr. 872; Caito, Tr. 1598), and many are produced on the same production line. (Williams, Tr. 104–05; Sack, Tr. 378; Lawrence, Tr. 664–68; Garber, Tr. 874, 1138; Caito, Tr. 1659.)

151. BOF bricks can be produced in the same plant and use some of the same equipment as other types of basic bricks. (Williams, Tr. 105, 212.) Some manufacturers produce BOF bricks on alternate runs with other basic bricks. (Williams, Tr. 105; Garber, Tr. 874, 1138.) Such a shift takes between a half-hour and forty-eight hours. (Williams, Tr. 105; Garber, Tr. 1138; Caito, Tr. 1659.)

152. Some specialized equipment is necessary for the production of BOF bricks, including mixers and presses used to keep coal tar in a liquid form and tar impregnators. (Williams, Tr. 105, 212; Sack, Tr. 385.)

153. To produce tar bonded bricks at a plant equipped to make direct bonded bricks, it costs about one-half million dollars. The additional equipment to produce tar impregnated bricks costs about $600,000. (Williams, Tr. 110.)

154. The five major types of basic bricks are produced by using the same raw material storage bins, batch cars, and crushing, grinding, sizing, mixing and pressing equipment. (Williams, Tr. 111; Sack, Tr. 376–79; CX 111Z10.) Some of the products use different finishing ovens. (CX 141.) **[30]**

155. In allocating production facilities among the types of basic bricks, refractories manufacturers predict production levels in consuming industries—primarily the steel industry. (CX 115I–L; CX 119A–M.)

156. Steel companies buy more than 80 percent on a dollar basis of all basic refractories bricks. (Garber, Tr. 880; Burriss, Tr. 1433; Caito, Tr. 1668–70; CX 221D; RX 132I.) They buy all of the major types of basic bricks. (Garber, Tr. 880; Kappmeyer, Tr. 1268; Burriss, Tr. 1433; Caito, Tr. 1668–69.)

157. An assured supply of magnesia is a prerequisite for effective competition in the basic brick refractory market. (Williams, Tr. 174; Sack, Tr. 431; Rook, Tr. 606; Garber, Tr. 1004; Gaydos, Tr. 1222; Hegeman, Tr. 1694–1700; Hall, Tr. 2260–63.) Basic brick manufacturers obtain magnesia either through vertical integration into magnesia production (Sack, Tr. 431–33) or through long-term supply contracts. (Rook, Tr. 642, 694; Hummer, Tr. 778.) In 1973, Kaiser and Harbison-Walker were the only basic refractories manufacturers which had completely integrated magnesia facilities. (CX 56"O".)

158. Basic brick producers follow the price leadership of Harbison-Walker. (Williams, Tr. 193–94; Lawrence, Tr. 699; Gaydos, Tr.

1202; Burriss, Tr. 1488; Mitsoff, Tr. 1770; Smith, Tr. 1821; Knight, Tr. 2427; Garber, Tr. 916.)

159. Basic bricks are recognized by steel producing companies and by refractories manufacturers as a separate product market. (Williams, Tr. 100; Lawrence, Tr. 641; Garber, Tr. 860; CX 113H; CX 178L; CX 219; CX 221B; CX 253Q.) Kaiser keeps different financial reports for basic bricks and for nonbasic bricks (CX 31; CX 41; CX 51D; CX 102), and recognizes basic bricks as one of the major refractories market sectors. (CX 56M.) [31]

D. BOF Bricks

160. BOF bricks are basic refractory bricks containing coal tar pitch ("tar"). There are two categories of BOF bricks: tar impregnated basic bricks, and tar bonded basic bricks. (Williams, Tr. 98; Sack, Tr. 374; Garber, Tr. 868; Lawrence, Tr. 873; Kappmeyer, Tr. 1294; Caito, Tr. 1657; CX 111G–H.)

161. Tar bonded and tar impregnated bricks are substitutable in the lining of basic oxygen steel-making furnaces. (Williams, Tr. 142; Lawrence, Tr. 673; Gaydos, Tr. 1182.)

162. Steel companies decide whether to purchase either tar bonded or tar impregnated bricks, based in part on the price of those products. (Williams, Tr. 142; Sack, Tr. 400; Hummer, Tr. 761.)

163. In 1973, almost all tar bonded and tar impregnated bricks were used in BOF's. (Williams, Tr. 267; Sack, Tr. 375, 397; Garber, Tr. 861, 886; Kappmeyer, Tr. 1296; Caito, Tr. 1667; CX 20M; CX 149D.)

164. BOF bricks vary in prices and quality. Advancing from the lowest in price and quality to the highest are tar bonded dolomite bricks, tar bonded dolomite and magnesia combinations, tar bonded magnesia and tar impregnated magnesia. (Sack, Tr. 400–01; Hummer, Tr. 761; Garber, Tr. 869–70; Gaydos, Tr. 1184; Caito, Tr. 1633.)

165. There is a trend towards an increase in the use of tar bonded bricks and a corresponding decrease in the use of tar impregnated bricks. This trend has resulted because of an increase in the quality of tar bonded bricks. (Sack, Tr. 400; Gaydos, Tr. 1184; Kappmeyer, Tr. 1300.)

166. Tar bonded bricks are made of magnesia and dolomite, and combinations thereof. (Williams, Tr. 138; Sack, Tr. 386; Lawrence, Tr. 678; Gaydos, Tr. 1180; Kappmeyer, Tr. 1294; Caito, Tr. 1657.) The raw materials are chemically bonded together with tar added at the mixing stage. (Williams, Tr. 142; Sack, Tr. 338–84; Garber, Tr. 861; CX 111H; RPF 24.) [32]

167. There is a trend away from the use of tar bonded dolomite bricks to the use of tar bonded magnesia brick in basic oxygen

furnaces. An increase in the price of dolomite would accelerate that trend. (Williams, Tr. 142; Sack, Tr. 400; Hummer, Tr. 760–61; CX 272A–B.)

168. Tar bonded bricks are sometimes tempered (*i.e.*, subjected to temperatures of between 300° and 800° F) to remove the volatiles from the tar and to avoid softening of the bricks in service. (Sack, Tr. 386; Garber, Tr. 862; RPF 24.)

169. Tar impregnated bricks in 1973 were made only of 100 percent magnesia. They are made by placing magnesia burned or bonded bricks in an autoclave to remove the air from the pores. The pores are then filled under pressure with hot tar. (Garber, Tr. 863; RPF 24.)

170. All working linings in BOF's are made of tar impregnated or tar bonded basic bricks. (Sack, Tr. 397; Lawrence, Tr. 678; Caito, Tr. 1671; Kappmeyer, Tr. 1295.)

171. Only basic bricks are used in BOF's. (Sack, Tr. 397; Lawrence, Tr. 674; Gaydos, Tr. 1184–85.) The basic slag which develops in the BOF during the steel-making process would destroy a nonbasic refractory. (Sack, Tr. 527.)

172. In 1973, 100 percent of all refractory bricks used in BOF's were tar bonded or tar impregnated basic bricks. (Sack, Tr. 397; Kappmeyer, Tr. 1270.)

173. In 1973, tar bonded and tar impregnated bricks not used in BOF's were only being used on a trial or experimental basis in working bottoms or subhearths of electric arc furnaces and in tundishes.[9] (Williams, Tr. 150, 159; Kappmeyer, Tr. 1296; Caito, Tr. 1622.)

174. Prior to the acquisition, both Kaiser and Lavino manufactured tar impregnated and tar bonded bricks. (Sack, Tr. 438; Lawrence, Tr. 691; Garber, Tr. 898; Gaydos, Tr. 1197; Burriss, Tr. 1429–30; Caito, Tr. 1629; CX 90"O"; CX 95Z73; CX 114K–L; CX 116G; CX 122; CX 123A–D.) Both companies were stepping up their marketing efforts in BOF bricks (Burriss, Tr. 1469; Hall, Tr. 2229; CPF 109; RPF 113) and forecasted increasing market penetration. (Burriss, Tr. 1469; CX 18; CX 21.) [33]

175. BOF bricks have continually improved. The consumption rate for refractory bricks in the working linings of BOF's dropped from approximately 19 pounds of refractory bricks per ton of steel in 1961 to about 4.1 pounds per ton of steel in 1973. (RPF 64; RX 249.) In 1977, the consumption rate was about 2.7 pounds per ton of steel. (RPF 64; RX 249.)

[9] A "tundish" is a large bathtub type vessel holding molten steel to be metered out into a continuous caster (Williams, Tr. 123.)

176. BOF bricks are recognized by steel producing companies and by refractories sellers, including Kaiser, as a distinct product market. (Sack, Tr. 374; Garber, Tr. 868; Gaydos, Tr. 1179; CX 16A–B; CX 17A; CX 21A–C; CX 41; CX 114A–L; CX 206Z46.) In 1971, Kaiser recognized BOF bricks as a "critical market." (CX 18.) Kaiser recognized that prices of BOF bricks were set without regard to prices of other basic or nonbasic bricks. (CX 32G.)

177. Both steel producing companies and refractories manufacturers recognized that Lavino and Kaiser were competitors in 1973 in the sale of BOF bricks. (Williams, Tr. 169–72; Sack, Tr. 438; Lawrence, Tr. 691; Hummer, Tr. 759–60; Garber, Tr. 897; Gaydos, Tr. 1197; Burriss, Tr. 1442–43; Mitsoff, Tr. 1768; CX 204Z144.) Lavino recognized that Kaiser was one of the four principal competitiors in this market. (CX 111L.)

178. In 1972, Lavino sold BOF products to 19 steel plants, as many as the other top three BOF suppliers. During that year, Kaiser sold these products to three of the same BOF plants supplied by Lavino. (CX 114H–J; CX 123B–D.) Lavino products were purchased by six of the top ten BOF steel companies. (CX 114C.) Lavino's BOF bricks were reported in 1971 by Kaiser to be "establishing records in the industry." (RX 132L.) Kaiser acknowledged that they were an established BOF supplier prior to the acquisition. (CX 18; CX 111L.) In 1973, Kaiser planned a 50 percent increase in sales volume of its BOF bricks because of an improvement in the quality of its product. In 1972, Kaiser sold as many BOF bricks as it could produce. (CX 32G.) Kaiser and Lavino both sold BOF products to four of the same steel companies in 1972. (CX 123B–D.) [34]

E. Conventionally Bonded Basic Bricks

179. There are three categories of conventionally bonded bricks: chemically bonded bricks, regular burned bricks and direct bonded bricks. (Williams, Tr. 98; Sack, Tr. 374; Garber, Tr. 861; Mitsoff, Tr. 1744; CX 116Z2; CX 230Z11–Z40; CX 253G; CX 952Z71–Z90.) These categories of basic bricks are used in the refractories industry. (CX 113H; CX 221F.) Kaiser also recognized and used these three categories. (CX 32C–D; CX 40.)

180. More than 95 percent of all conventionally bonded bricks are manufactured from magnesia, chrome ore, or combinations thereof. (Sack, Tr. 374; Lawrence, Tr. 642; Garber, Tr. 859; Gaydos, Tr. 1177; CX 95; CX 139; CX 205Z3–Z4.)

181. Less than 5 percent of all conventionally bonded bricks are manufactured from dolomite. (CX 139.) Dolomite has a shorter shelf

and furnace life than magnesia. The price of dolomite depends on the price of magnesia. (Sack, Tr. 404; Hummer, Tr. 780; CX 272.)

182. The quality and the price of magnesia/chrome ore conventionally bonded bricks depends upon the ratio of magnesia to chrome ore (Williams, Tr. 127), upon the grade of magnesia and chrome ore (Lawrence, Tr. 712; Van Dreser, Tr. 2686–90), and upon the method of bonding the raw materials together. (Williams, Tr. 127.)

183. Generally, the cheapest and least durable conventionally bonded basic brick is the chemically bonded brick in which the raw materials are bonded together by chemical additives.[10] (Williams, Tr. 127, 146; Sack, Tr. 375; Lawrence, Tr. 679–80; Garber, Tr. 887; CX 111G.)

184. A more expensive and more durable conventionally bonded brick is the regular burned brick in which the basic raw materials are bonded together by firing the brick in a kiln at temperatures of about 2750°–2900°F.[11] The firing creates a ceramic bond. (Williams, Tr. 127, 146; Sack, Tr. 376; Lawrence, Tr. 679–80; Garber, Tr. 861, 887.) [35]

185. The most expensive and durable conventionally bonded brick is the direct bonded brick in which the basic raw materials are bonded together by firing the brick in a kiln at temperatures of about 3200° F and above.[12] The firing creates a direct bond between the magnesia and the chrome ore. (Williams, Tr. 146–57; Sack, Tr. 375; Garber, Tr. 861, 867; Adams, Tr. 2590–91.)

186. Each of the types of conventionally bonded bricks may be produced interchangeably on the same production line in a plant with a high firing capacity kiln. In 1973, six of the manufacturers of basic bricks had this capacity. (RPF 305; Williams, Tr. 105; Sack, Tr. 377–79; Lawrence, Tr. 658–68; Garber, Tr. 864–65, 1137; CX 64C; CX 118Z2; CX 168L–P.) The basic raw materials for each type are crushed and ground in the same ball and rod mills, and mixed and pressed into shapes in the same mixers and presses. (Williams, Tr. 105; Sack, Tr. 377–78; Lawrence, Tr. 656–68; Garber, Tr. 874.)

187. Shifting production from one type of conventionally bonded brick to another requires a change in the raw materials and a change in the temperature at which the brick is fired. (Sack, Tr. 379; Lawrence, Tr. 660–62; Garber, Tr. 864, 1137.) General Refractories varies its production of regular burned, direct bonded and chemically bonded basic bricks, on the same facilities, up to twenty times a year to meet demand. (Lawrence, Tr. 664–68.)

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[10] Chemically bonded bricks are also called "unburned." (CX 32C.)

[11] Regular burned bricks are also called "burned" (CX 32C) and "conventional burned." (CX 218.)

[12] Direct bonded bricks are also called "high fired." (CX 221F.)

188. To change the kiln temperature from direct bond temperatures to regular burned temperatures takes five to eight hours and from regular burned temperatures to direct bond temperatures twelve to twenty-four hours. (Williams, Tr. 108; Garber, Tr. 1137.)

189. It costs several millions to add high firing kiln capacity to convert a plant producing chemically bonded bricks to a plant producing direct bonded bricks. (Garber, Tr. 929.) **[36]**

190. Most basic brick manufacturers produce chemically bonded, regular burned and direct bonded bricks. (Williams, Tr. 94; Sack, Tr. 375–76; Lawrence, Tr. 647–49; Garber, Tr. 870–71; RPF 305.) The capacity of the plants varies depending upon the specific product mix at any given time. (Williams, Tr. 111; Hummer, Tr. 758; Garber, Tr. 875; CX 22G; CX 64C; CX 168C–K; CX 273.)

191. Nonbasic bricks are not produced on the same production line as conventionally bonded basic bricks (Sack, Tr. 373; Lawrence, Tr. 650) and rarely are they produced in the same plant. (Williams, Tr. 94; Caito, Tr. 1661.)

192. About half of the conventionally bonded basic bricks are sold to the steel industry. (CX 20N.) Over 90 percent of these bricks are used in the working or safety linings of OHF's, EAF's and AOD's. (Lawrence, Tr. 679; Kappmeyer, Tr. 1270, 1277.)

193. The rest of the conventionally bonded bricks are used in various other industrial applications, including burning zones of cement kilns (Lawrence, Tr. 685; Garber, Tr. 890), copper reverberators (Lawrence, Tr. 686; Garber, Tr. 892–93) and the checkers of glass furnaces. (William, Tr. 253; Sack, Tr. 472; Lawrence, Tr. 686; Garber, Tr. 890; CX 113H.)

194. There is a trend towards using direct bonded basic bricks where regular burned bricks were previously used (Williams, Tr. 127, 148; Sack, Tr. 409; CX 66J) because furnace operators are demanding increasing lining lives. (Sack, Tr. 411; Garber, Tr. 975; Adams, Tr. 2590; CX 255.)

195. Fused cast basic bricks are used in OHF's, EAF's and AOD's. (Sack, Tr. 392; Garber, Tr. 882; Ackerman, Tr. 1854–55.) In 1973, this product was produced only by Corhart Refractories Co. (Williams, Tr. 131; Sack, Tr. 393; Ackerman, Tr. 1890–91.)

196. The fused cast basic brick is manufactured by an entirely different process than regular burned, chemically bonded and direct bonded bricks. Fused cast bricks are made by fusing refractory raw materials together into a liquid, pouring the molten material into a mold, letting it cool, and sawing brick shapes from this cooled mass. (Williams, Tr. 131; Sack, Tr. 393; Ackerman, Tr. 1853.) **[37]**

197. Fused cast bricks are so expensive in relation to other basic

bricks that in 1973 they were used only at the slag lines and hot spots of some steel-making furnaces. (Garber, Tr. 1147; Ackerman, Tr. 1928; CX 269B.) Recently, this application of fused cast bricks has been diminished by the use of water cooled side panels and PMT bricks in EAF's. (Williams, Tr. 238; Garber, Tr. 1147; Ackerman, Tr. 1869–70.)

198. In 1973, BOF bricks were not substituted for conventionally bonded basic bricks. (Lawrence, Tr. 685.) BOF bricks would not be functional in most applications where conventionally bonded bricks are used because, for instance, in AOD's the tar in BOF bricks would be burned out leaving only granular magnesia. (Sack, Tr. 406; Garber, Tr. 939–41.)

199. In 1973, nonbasic bricks were not used in place of conventionally bonded basic bricks except in a few minor applications including burning zones of rotary kilns (Williams, Tr. 165; Burriss, Tr. 1436), regenerators of glass furnaces (Burriss, Tr. 1436), ladles and tundishes (Williams, Tr. 164; Sack, Tr. 459; Kappmeyer, Tr. 1316; Burriss, Tr. 1434), and in some EAF roofs (Williams, Tr. 164, 263; Sack, Tr. 458–59; Burriss, Tr. 1435.) When a cold charge is used in an EAF, the roof must be made of basic refractories because slag reaches the roof; when a hot charge is used, the cheaper nonbasic roof can be used since the slag does not then reach the roof of the furnace. (Williams, Tr. 275.) More EAF's now have basic roofs than in 1973. (Williams, Tr. 148.)

200. Basic refractories manufacturers, including Kaiser, recognize and keep separate financial records (sales, costs, profits) for direct bond, regular burn, and chemically bond basic bricks. (CX 32B; CX 40; CX 113H; CX 218; CX 219; CX 247; CX 253Q.)

201. Both Kaiser and Lavino produced chemically bonded, regular burned and direct bonded basic bricks (Lawrence, Tr. 701; Garber, Tr. 896, 1106–07; Gaydos, Tr. 1195–96; Burriss, Tr. 1439; Knight, Tr. 2425) for use in the steel-making (Williams, Tr. 283–86; Lawrence, Tr. 701; Gaydos, Tr. 1198; Burriss, Tr. 1440–41), glass and copper industries. (Lawrence, Tr. 701; Garber, Tr. 897; Burriss, Tr. 1440–41; Knight, Tr. 2425–26.)

202. Both steel producing and refractories companies recognized that Lavino and Kaiser were competitiors in 1973 in the sale of chemically bonded, regular burned and direct bonded bricks. (Sack, Tr. 437; Garber, Tr. 896; Gaydos, Tr. 1195–96; CX 248.) [38]

Market Behavior

A. Barriers to Entry

203. There have been no new entrants into the basic refractories market since 1964. (Williams, Tr. 185; Kappmeyer, Tr. 1336.)

204. In 1973, there were no potential entrants into the basic refractories market. (Williams, Tr. 186; Lawrence, Tr. 696; Garber, Tr. 898; Gaydos, Tr. 1203; Kappmeyer, Tr. 1337, 1404; Burriss, Tr. 1445.)

205. Steel companies are not perceived by manufacturers of basic refractories to be potential entrants into the production of basic refractories. (Williams, Tr. 189–90; Lawrence, Tr. 698; Garber, Tr. 898; Burriss, Tr. 1445; Caito, Tr. 1672–73, 1686–87.)

206. It would cost about $50 million to $60 million to build an efficient full-line basic refractories plant. (Garber, Tr. 901; Hegeman, Tr. 1710.)

207. The minimum amount of sales per year necessary to be profitable in the basic refractories market was about $12 million in 1973. (Williams, Tr. 362.)

208. It takes three to five years to enter into the production of basic refractories. This amount of time is necessary in order to build a plant, to develop products, to supply the products to the R&D departments of the steel companies and for steel companies to test the products in production furnaces. (Rook, Tr. 577–78.)

209. An innovative R&D department is essential to the success of a basic refractories manufacturer. (Williams, Tr. 182, 322, 362; Lawrence, Tr. 719, 735; Hummer, Tr. 779; Garber, Tr. 902; Burriss, Tr. 1454.) Consistently high quality products are of major competitive importance in the basic refractories industry. In addition to quality control, constant upgrading of products is necessary. (Williams, Tr. 322, 338–39; Lawrence, Tr. 719–20; Van Dreser, Tr. 2677; CX 13I.) A new entrant into the basic refractories market would ıave to have high quality R&D to be successful. (Lawrence, Tr. 697.) Kaiser's 1966–1977 Strategic Plan concluded that R&D "pre-investıent costs are substantial and probably preclude new entrants into ıe industry." (CX 12T.) [39]

210. The R&D departments of major steel companies themselves ɜt and evaluate basic refractory products. (Lawrence, Tr. 720; ydos, Tr. 1231; Kappmeyer, Tr. 1340–42, 1363–65.)

'11. The R&D departments of the major steel companies formu- specifications regarding the quality of basic refractory products ch must be met in order for the steel operators to be allowed to :hase a particular product. (Garber, Tr. 1142; Gaydos, Tr. 1231– Kappmeyer, Tr. 1340–42, 1363–65.)

2. Once a steel company's R&D department has approved a in basic refractory product, the furnace operators select from

products on the approved list. (Gaydos, Tr. 1231–33; Kappmeyer, Tr. 1340–42; CX 110B; CX 256D–E.) The furnace operators develop loyalties to specific products and are reluctant to change to untried products. (CX 12Q.) As Kaiser recognized in their 1966–1977 Strategic Plan Outline: "This can be a barrier to entry of new refractories companies." (CX 12Q.)

B. History and Future of the Industry

213. The number of refractories producers in the United States declined from 179 in 1956 to 97 in 1976. (RX 10B; RX 27C.) This trend is primarily due to the shift from the use of nonbasic to basic refractories (CX 180Z24.) Smaller companies making nonbasic refractories were not equipped technologically or financially to develop the high performance refractories now demanded. (CX 181X.)

214. The increased quality and life of refractories products has meant fewer sales but higher cost and prices and increasing dollar sales by refractories producers. (Sack, Tr. 409–10; CX 180K, Z24, Z36; CX 181Q.) Because of increasingly severe processes, such as the growing use of AOD and electric furnaces, more basic refractories will be used in the future. (Sack, Tr. 411; CX 255.) [40]

215. Many plants producing nonbasic refractories have been abandoned rather than switched to the production of basic refractories. Most new plants have been built for basic brick production. (CX 181Y.)

216. In the early 1960's, most basic refractories producers were independent companies. A wave of mergers occurred and almost all major basic refractories manufacturers became subsidiaries or divisions of large corporations having annual sales of at least $400 million. (Williams, Tr. 94; Sack, Tr. 371; Rook, Tr. 542; Garber, Tr. 857; Hegeman, Tr. 1690; CX 56N–P; CX 116B; CX 117C.) Of the top ten basic refractories manufacturers, only Basic, Inc., and General Refractories Company remain independent. (CX 117C.)

217. In 1968, Kaiser viewed these mergers as having a "positive influence" on profitability in the refractories industry (CX 13J) and as accelerating a trend toward "price firming as evidenced by Harbison-Walker leadership." (CX 13K.)

218. Kaiser and other refractories companies, as well as their primary customers, the steel companies, recognize that fewer refractories companies in the industry are likely to result in higher prices for basic refractory products. (CX 12P; CX 101B.)

219. Historically there has been little price competition in the basic refractories industry. At least as far back as the early 1930's

when the NRA (National Recovery Administration) existed, the practice in the basic refractories industry has been for one company to set prices and for all other industry members to follow these prices. (Williams, Tr. 190–91; Lawrence, Tr. 699; Garber, Tr. 918; Gaydos, Tr. 1201; Hall, Tr. 2313–14.)

220. Uniform prices are maintained in the basic refractories industry. (Mitsoff, Tr. 1773; Young, Tr. 1821; Smith, Tr. 2851.) The freight equalization method of pricing (*i.e.*, absorbing freight costs in selling prices to meet the price of more closely situated producers) is used in the industry. (Williams, Tr. 191; Garber, Tr. 1066–67.) Manufacturers of basic refractories publish price lists of their products (Williams, Tr. 190; Lawrence, Tr. 698–700; Garber, Tr. 1064) and very rarely fluctuate from those prices. (Gaydos, Tr. 1202; Smith, Tr. 2850.) [41]

221. Steel companies traditionally receive a "steel discount" amounting to 7 1/2 percent from their suppliers. Basic refractories manufacturers do not grant this discount to steel companies. (Williams, Tr. 192.)

222. Major basic refractories manufacturers which own their own source of supply of magnesia, supply their own needs and sell magnesia to smaller basic refractories manufacturers.[13] The smaller manufacturers sometimes lose their source of raw materials when they attempt to compete with their supplier in the finished refractory. (Hegeman, Tr. 1699–1701.)

223. In 1977, NARCO acquired another basic refractories manufacturer, H. K. Porter Company. (Williams, Tr. 171, 361.) The president of NARCO testified that NARCO decisions on future acquisitions of basic refractories companies will depend on the outcome of this litigation. (Williams, Tr. 347–48.) Martin Marietta is also watching. (CX 213Z11–13.)

Anticompetitive Effects

A. Elimination of Actual Competition between Kaiser and Lavino

224. Prior to the acquisition, Kaiser and Lavino were in direct competition with one another in the manufacture and sale of basic refractories to the same consumers. (CX 19E–H.)

225. Lavino in 1973 manufactured and sold a full line of basic refractories including direct bonded brick, chemically bonded brick, regular burned brick, tar bonded brick, tar impregnated brick and basic specialties. Kaiser in 1973 also manufactured and sold a full

[13] See Finding 157.

line of basic refractories including direct bonded brick, chemically bonded brick, regular burned brick, tar bonded brick, tar impregnated brick and basic specialties. (Burriss, Tr. 1480; CX 95A-Z314; CX 116H; CX 204Z71-Z79, Z81-Z84.)

226. In fiscal year 1973, Lavino sold basic refractories to customers which also purchased basic refractories from Kaiser in calendar year 1973. These sales by Kaiser amounted to more than $19 million and by Lavino amounted to more than $17 million; in both cases this was over one-half of their total basic sales. (CX 38A-Q, *in camera;* CX 78A-S; CX 138D, F; CX 168H-I.) [42]

227. In fiscal year 1973, Lavino sold basic refractory bricks to nine out of Kaiser's top ten refractory customers for calendar 1973. The only such customer which did not purchase refractories from Lavino during its fiscal year 1973 was Electro Refractoraire, Kaiser's French affiliate. (CX 168K.)

228. In 1973 and before the acquisition, Kaiser and Lavino were significant competitors in the sale of basic refractory products to the steel industry, the cement industry, the copper industry and the glass industry for each of Kaiser's and Lavino's basic products. (Lawrence, Tr. 701; Burriss, Tr. 1436-37; CX 19G-H; CX 64M-N; CX 110I; CX 111L, Z17; CX 115I; CX 116G; CX 117H-I, L; RX 495—Herbst 96, 116, 153-55.)

229. The major steel companies regarded Kaiser and Lavino as competitors for all types of basic brick and specialties in 1973. (Gaydos, Tr. 1195-1200; Kappmeyer, Tr. 1324-25; Mitsoff, Tr. 1735, 1741-42; Young, Tr. 1792, 1809; RX 495—Herbst 116, 153-55.) In that same year the major steel companies purchased basic refractory products from both Kaiser and Lavino for applications in open hearth, electric arc and basic oxygen furnaces. (Garber, Tr. 1106-08; Gaydos, Tr. 1197-99; Kappmeyer, Tr. 1324-25; CX 116G.)

230. Basic refractory producers viewed Kaiser and Lavino as competitors with each other and with themselves and other basic refractory producers in 1973 in the production and sale of tar impregnated basic brick, tar bonded basic brick, chemically bonded basic brick, regular burned basic brick, direct bonded basic brick and basic specialties. (CX 140A-L, *in camera;* CX 246C; CX 248A-B, *in camera;* CX 264; RX 495—Herbst 48-49, 96, 104, 120-21, 153-55; Williams, Tr. 169-71; Sack, Tr. 436-40; Rook, Tr. 548; Lawrence, Tr. 690-92; Hummer, Tr. 759-60, 765-66; Garber, Tr. 896-97, 1106-08; Burriss, Tr. 1439-43; Caito, Tr. 1628-29; Knight, Tr. 2426-27.)

231. Lavino viewed itself as a competitor with Kaiser in 1973 and before in the production and sale of direct bonded basic brick, chemically bonded basic brick, regular burned basic brick, tar

bonded basic brick, tar impregnated basic brick and basic specialties. (Burriss, Tr. 1439-43; CX 116G-H; CX 136B; RX 495—Herbst 104.) [43]

232. In 1973 and before, Kaiser viewed Lavino as a competitor in all categories of basic refractories in all areas of the United States. (CX 13I; CX 19C-D; CX 26C; CX 28A; CX 50; CX 56N; CX 60B-D, H-O; CX 66M.)

233. Kaiser was aware of Lavino's prices for basic refractory products and, in at least one instance, lowered its own price to meet that of Lavino. (CX 28A.)

B. Structure of the Markets

1. Basic Refractories Market

234. Total sales of basic refractories in 1973 amounted to $284 million. In 1973, Kaiser and Lavino were the second and fourth largest producers of basic refractories. Kaiser had $33.8 million in production and sales in the market in 1973 which amounted to 11.9 percent. Lavino had $26.4 million in production and sales which amounted to 9.3 percent. (CX 138A-F; CX 139A-X.)

235. Concentration in the basic refractories market was high in 1973 with the top firms having 33 percent, the top four firms having 53 percent and the top eight having 84 percent. (CX 138A-F; CX 139A-X.)

236. As a result of the acquisition, two firm concentration increased 9.3 percentage points, four firm concentration increased 9.1 percentage points and eight firm concentration increased 4.71 percentage points in the sale of basic refractories. In addition, the number four firm was eliminated. (CX 138A-F; CX 139A-X):

	1973 Pre-Acquisition	*1973 Post-Acquisition*	*Percent Increase*
Two firm	33.18	42.48	28.03
Four Firm	53.06	62.16	17.15
Eight Firm	83.80	88.51	5.62
Kaiser (rank)	11.87 (2)	21.18 (2)	78.43
Lavino (rank)	9.30 (4)	---	---

[44] 2. Basic Specialties Market

237. Total sales of basic refractory specialties were $90 million in 1973. In that year Kaiser was the third largest domestic producer of basic specialties, having nearly 15 percent of that market with $13.5 million in production and sales. Lavino was a substantial manufac-

turer of basic specialties with sales of $2.85 million, having 3 percent of production and sales of basic specialties. (CX 138A–F; CX 139A–X.)

238. Concentration in the basic specialties market was high in 1973, with the top two firms having 37 percent of sales, the top four firms having 67 percent of sales and the top eight having 88 percent. (CX 138A–F; CX 139A–X.)

239. As a result of the acquisition, two firm concentration in the sale of basic refractory specialties increased by 2 percentage points while four firm and eight firm concentration each increased 3.13 percentage points. In addition, Kaiser became the number two firm, moving up from number three, and a substantial competitor in the market was eliminated. (CX 138A–F; CX 139A–X):

	1973 Pre-Acquisition	*1973 Post-Acquisition*	*Percent Increase*
Two Firm	37.49	39.50	5.36
Four Firm	67.01	70.14	4.67
Eight Firm	88.30	91.43	3.54
Kaiser (rank)	14.82 (3)	17.95 (2)	21.12
Lavino (rank)	3.13 (9)	—	—

[45] 3. Basic Refractory Bricks Market

240. Total sales of basic refractory bricks were $194 million in 1973. In that year Lavino and Kaiser were the third and sixth largest producers of basic refractory bricks. Lavino had $23.6 million of production and sales in the market in 1973 which amounted to 12.2 percent. Kaiser had $20.3 million in production and sales which amounted to 10.5 percent. (CX 138A–F; CX 139A–X.)

241. Concentration was high in the basic refractory bricks market with the top two firms having 41 percent, the top four firms having 65 percent and the top eight firms having 94 percent of total sales of basic refractory bricks in 1973. Only 13 firms manufactured basic refractory bricks in 1973. (CX 138A–F; CX 139A–X.)

242. As a result of the acquisition, two firm concentration in the sale of basic refractory bricks increased by 9.6 percentage points, four firm concentration increased 10.5 percentage points and eight firm concentration increased by 2.39 percentage points. In addition, the number three firm was eliminated and Kaiser moved from being the number six firm to become the number two firm in that market. (CX 138A–F; CX 139A–X):

	1973 Pre-Acquisition	*1973 Post-Acquisition*	*Percent Increase*
Two Firm	41.35	50.92	23.14
Four Firm	64.68	75.18	16.23

Eight Firm	94.29	96.68	2.53
Kaiser (rank)	10.49 (6)	22.70 (2)	116.40
Lavino (rank)	12.20 (3)	—	—

[46] 4. BOF Basic Bricks Market

243. Total sales of BOF basic bricks were $45 million in 1973. In that year, Lavino and Kaiser were the fourth and sixth largest producers of BOF basic bricks. Lavino had $3.6 million in production and sales in the market in 1973 amounting to 8 percent. Kaiser had $1.75 million in production and sales which amounted to 4 percent. (CX 138A–F; CX 139A–X.)

244. Concentration was high in the BOF basic bricks market with the top four firms having 81 percent and the top eight firms having 98 percent of total sales in 1973. Only 9 firms manufactured BOF basic bricks in that year. (CX 138A–F; CX 139A–X.)

245. In the sale of BOF basic bricks, the acquisition caused four firm concentration to increase by 3.98 percentage points and eight firm concentration also to increase. The number four firm in the industry was eliminated and Kaiser became number four, moving up from number six. (CX 138A–F; CX 139A–X):

	1973 Pre-Aquisition	*1973 Post-Aquisition*	*Percent Increase*
Four Firm	81.46	85.44	4.89
Eight Firm	98.35	99.97	1.65
Kaiser (rank)	3.97 (6)	12.07 (4)	204.03
Lavino (rank)	8.09 (4)	—	—

[47] 5. Conventionally Bonded Basic Bricks Market

246. Total sales of conventionally bonded basic bricks were $132 million in 1973. In that year, Lavino and Kaiser were the second and fourth largest producers of conventionally bonded basic bricks. Lavino had $20 million of production and sales in the market in 1973, amounting to 15.17 percent. Kaiser had $18.6 million in production and sales which amounted to 14.04 percent. (CX 138A–F; CX 139A–X.)

247. Concentration was high in the conventionally bonded basic bricks market with the top two firms having 46 percent, the top four firms having 76 percent and the top eight firms having 97 percent of total sales in 1973. Only 10 firms manufactured conventionally bonded basic bricks in that year. (CX 138A–F; CX 139A–X.)

248. As a result of the acquisition, two firm concentration in the sale of conventionally bonded basic bricks increased by 14 percentage points, four firm concentration increased by 9.27 percentage

points, and eight firm concentration also increased. In addition, the number two firm was eliminated and Kaiser moved from number four to number two. (CX 138A-F; CX 139A-X):

	1973 Pre-Acquisition	*1973 Post-Aquisition*	*Percent Increase*
Two Firm	46.44	60.48	30.23
Four Firm	75.57	84.84	12.27
Eight Firm	96.87	99.57	2.79
Kaiser (rank)	14.04 (4)	29.22 (2)	108.05
Lavino (rank)	15.17 (2)	—	—

[48] DISCUSSION

The following discussion summarizes and supplements the findings of fact and presents conclusions of law.

Introduction

Refractories are insulating materials used to control heat. A brick in a home fireplace is a refractory, as is the nose cone on a space vehicle. But the biggest use of refractories is to line furnaces and other equipment used in producing glass, cement, copper and steel.

The refractories industry classifies refractories as acid or basic, depending on the raw material used. To minimize wear, the chemical reaction of the refractory must be the same as the material being insulated. Thus, an acid refractory would not be used where it would contact the slag in a steel-making furnace, since that slag is chemically basic.

Refractories are also classified by their physical form as bricks and specialties. Refractory bricks may be rectangular or another shape such as a tapered wedge which is more useful for building a curved wall or the roof of a furnace. Refractory specialties may be grains the size of garden peas or children's marbles, or may be like putty. Refractory bricks are applied by bricklayers who build the industrial surface the way they would build a brick house with common bricks. Applying specialties is more like laying concrete, and the material may be cast, tamped or trowelled into place or blown through a pneumatic gun.

Refractories wear out from the high temperatures, chemical attack and buffeting they receive in use. Constant maintenance by adding additional refractories is necessary. One witness described what occurs when this is not done (Williams, Tr. 353):

They have what they term in the steel industry a "break out." A break out is where the refractory fails and the steel shell of these BOF vessels is about, depending on the size of the vessel, 3 to 6 inches thick. But if this hot metal gets to the steel shell, it will burn a hole in the steel shell just like a melting torch and out squirts a thick stream of metal and that is a disaster.

[49] There is no substitute for refractories used to line industrial furnaces. For this reason, the refractory industry is highly important to the national economy.

Relevant Product Markets

This case involves an acquisition by respondent Kaiser of the refractories plants and assets of its competitor, the Lavino division of IMC. Both the Refractories Division of Kaiser and Lavino sold the same products to the same customers. They recognized each other as "major" competitors. (CX 56N; CX 111L.) After a careful study of Lavino, Kaiser's Refractories Division strongly recommended that the Lavino assets promptly be acquired, and one of the key elements for the proposed merger was that (CX 66M):

> The same products, the same customers, the same applications, the same territories, are already an integral part of KaRef operations for the majority of the product lines. Much of the present operating expenses of Company "X" are spent in duplication of KaRef established efforts.[14]

Lavino also recognized that Kaiser was a company selling "products that compete functionally" with its own products for use in each of the uses for basic refractories. (CX 116G–H.)

To test whether an acquisition may substantially lessen competition, the area of effective competition must be determined by reference to product markets. *Brown Shoe Co.* v. *United States,* 370 U.S. 294, 324 (1962). The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it. *Id.* at 325. Within the broad market, well-defined submarkets may exist which constitute product markets for antitrust purposes, and the boundaries of such submarkets may be determined by looking at, *id.* p. 325: [50]

> industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors.

Not all of these criteria must be met before a relevant submarket is found. Indeed, in *Brown Shoe* itself, the Court upheld the submark-

[14] Company "X" was Lavino. (Adams, Tr. 2473.)

ets of men's, women's and children's shoes based only on public recognition, separate production plants, peculiar product characteristics and distinct customers. 370 U.S. at 326. And in *United States* v. *Aluminum Co. of America,* 377 U.S. 271 (1964), the Court observed that aluminum and copper electrical conductors perform the same job equally well. 377 U.S. at 276. Nevertheless, the Court found the two in separate submarkets, relying on only two factors: distinctive characteristics and prices. *Id.* at 276–77.[15] The record in this case clearly establishes five "area[s] of effective competition," *United States* v. *Continental Can Co.,* 378 U.S. 441, 456 (1964), in which to test the competitive effects of this acquisition.[16] [51]

Basic Refractories

Most refractories manufacturers make and sell both basic and nonbasic refractories and their trade association is for all refractories companies. (CX 204.) There are a few uses where certain basic and nonbasic refractories are interchangeable, such as in the roofs of electric arc steel-making furnaces. But in this wider market for refractories, submarkets exist which constitute product markets for antitrust purposes.[17] Both aupply and demand side analyses show that basic refractories products constitute such a product market.

Basic refractories have peculiar characteristics, different from nonbasic refractories, which make them uniquely capable of insulating steel-making furnaces where the molten slag would quickly destroy any other product. (Findings 16, 96, 112.) Both forms of basic refractories—bricks and specialties—are used interchangeably for this purpose. (Findings 97–99, 129.)[18] The major basic refractories companies can produce all basic refractories products on the same

[15] See also, *Abex Corp.* v. *FTC,* 420 F.2d 928, 931–32 (6th Cir.), *cert. denied,* 400 U.S. 865 (1970); see other cases cited in *Reichhold Chemicals, Inc.*, Dkt. 9076 [91 F.T.C. 246], Initial Decision by Law Judge Needelman, at pp. 62–63 of slip opinion (unreported), adopted by the Commission, 3 CCH Trade Reg. Rep. ¶ 21,412 (Feb. 22, 1978), appeal pending, Fourth Circuit Court of Appeals # 78–1275.

[16] There is precedent in finding a relevant product market based on ingredients and a submarket based on use in the same case. In *United States* v. *Continental Can Co.*, 378 U.S. 441, 448, 457 (1964), the Supreme Court defined a market for the "combined glass and metal container industries and all end uses for which they compete," and did not reverse the finding of the district court that "containers for beer" was a submarket. Thus, it is permissible here to draw relevant product markets based on the outstanding characteristics of each market, *i.e.*, basic refractories, basic bricks and basic specialties being named for their ingredients, BOF bricks being named for the use of the products, and conventionally bonded bricks being named by the construction of the products. Other relevant product markets based on the way the products are made include artificial Christmas trees, *United States* v. *American Technical Industries, Inc.*, 1974–1 Trade Cases ¶ 74,873 (M.D. Pa. 1974), and frozen pies, *United States* v. *Mrs. Smith's Pie Co.*, 440 F. Supp. 220 (E.D. Pa. 1976). But see, *Sterling Drug, Inc.*, 80 F.T.C. 477, 599 n.24 (1972).

[17] Such submarkets may exist even though the broad market is not a product market for antitrust purposes. *Brown Shoe Company* v. *United States,* 370 U.S. at 299 (submarkets for men's, women's and children's shoes but not for all shoes); *Brunswick Corp.*, F.T.C. Dkt. 9028 (Initial Decision 5/2/77, at p. 66) (submarkets for high and low powered outboard motors but not for outboards).

[18] That both basic bricks and basic specialties are separate relevant product markets does not stop the broader basic refractories market from being a product market for antitrust purposes. *United States* v. *Phillipsburg National Bank,* 399 U.S. 350, 360 (1970); *United States* v. *Continental Can Co.*, 378 U.S. 441 456–57 (1964).

facilities at some of their plants. (RPF 305; Finding 103.) Not all basic refractories plants can produce all basic refractories but all of the major producers, including Lavino and Kaiser, possessed the machinery to produce all types of basic refractories. Completely interchangeable production facilities are not necessary to find that products are in the same relevant market. *Liggett & Myers Inc.,* 87 F.T.C. 1074, 1158 (1976), *aff'd,* 567 F.2d 1273 (4th Cir. 1977). Basic refractories [52] and nonbasic refractories are not produced in the United States on the same production lines. (Findings 104, 105.)[19] The major basic refractories producers sell both basic bricks and basic specialties. (Findings 100–03.)

Refractories producers themselves recognize basic refractories as an independent product market. (Findings 106–07.) And the technical knowledge for basic refractories is so distinct from nonbasic refractories that individuals specialize in developing, selling and buying basic refractories and do not deal in nonbasics. (Findings 110, 111, 113.)

Basic refractories are priced without regard to the prices of nonbasic refractories. (Findings 108, 109.) As a Lavino planning document stated, the use of basic refractories in the steel industry is required by the specifications of the steel companies and (CX 126D): "Other refractories products cannot meet these specifications so the cost of other products is not an important factor." Such supply side perceptions control the area of effective competition among products in the same market. *Reichhold Chemicals, Inc., supra* at p. 60 of unreported slip opinion. And while it is true as argued by Kaiser that not all basic refractories are fungible, nonhomogeneous products have been held to constitute a line of commerce where, as here, there is resource flexibility or the sale of a full line by many firms. *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 356 (1963); *Sterling Drug, Inc.,* 80 F.T.C. 477, 595 n.19 (1972) *(dicta).* [53]

Basic Specialties

Almost all basic specialties are used in the steel industry (Finding 115) in steel-making furnaces. (Finding 128.) Only basic specialties or basic bricks are used to line most steel-making furnaces. (Findings 16, 95, 112.) Basic specialties are the only product which can be used as a patching material for the basic refractories lining in those

[19] There is some proof in the record that the German company, Didier, can make basic and nonbasic refractories in the same plant. (Mahler, Tr. 3007–09.) Even where production facilities are completely interchangeable, however, the better rule is to rely on that factor in considering the outer boundaries of a market but merely to look at it—with other factors—when drawing submarkets. Where products have different customers, end uses and inelastic prices, separate product markets should be formed regardless of the interchangeability of production facilities. *Budd Co.,* 86 F.T.C. 518, 567 n.1 (1975) (dissenting statement of Commissioner Dixon).

furnaces to avoid a "break out" (Findings 97, 99, 129) and may be sprayed on by a pneumatic gun while the furnace is still hot. (Finding 98.)

Basic specialties have industry recognition as a separate product line. (Findings 132, 133.) Basic specialties can be produced on some of the same equipment as basic bricks, but are not made on equipment used to make nonbasic specialties in the United States. (Findings 124, 126, 127.) Basic specialties have distinct customers—the steel industry. Specialized individuals (different from those who buy nonbasic refractories and from those who buy basic bricks) buy basic specialties for steel-making furnaces. (Findings 113, 130.) The price leader for basic specialties is different from the price leader for basic bricks and prices for basic specialties are set without taking account of prices for nonbasic products. (Finding 131.)

Basic Bricks

More than 80 percent of all basic bricks are sold to the steel industry for use in steel-making furnaces. (Finding 156.) Almost all of the brick refractories used in the steel-making furnaces in this country are basic. (Findings 95, 171, 172, 199.) Nonbasic refractories do not have the same characteristics and are not used for these same purposes. (Finding 143.) While basic specialties and basic bricks can be used interchangeably (Findings 97-99, 129), the products are usually used as complements (brick to build and specialties to patch), and not as substitutes. [54]

All major types of basic bricks (chemically bonded, regular burned, direct bonded, tar bonded and tar impregnated) can be made on the same production line of a well-equipped plant and major refractories manufacturers alternate production of the types of such bricks to meet demand. (Findings 150, 151, 154.) Nonbasic bricks are not usually produced at the same plant that produces basic refractories. (Finding 144.) Research and development is a critical aspect of producing basic bricks. (Findings 146-148.) R&D expertise in basic bricks production is not applicable to nonbasic refractories. (Findings 110, 141, 142.)

Prices for basic bricks are set without regard to the price of basic specialties and different refractories producers are the price leaders in each market. (Findings 131, 158; CX 56Q.) Basic bricks are recognized as a distinct product market by steel companies and by refractories manufacturers. (Finding 159.)

BOF Basic Bricks

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Cross-elastic demand and interchangeable use show that BOF bricks are a relevant product market. BOF furnaces, which make most of the steel produced in this country, use only basic bricks bonded or impregnated with tar. (Findings 95, 171, 172.) Almost all basic bricks bonded or impregnated with tar were used in BOF's in 1973. (Finding 163.)

BOF bricks are recognized as a distinct product market by steel companies and refractories manufacturers. (Finding 176.) BOF bricks are priced without regard to the price of other basic or nonbasic bricks. (Finding 176.) "These preferences on the demand side and perceptions on the supply side combine to form an 'area of effective competition.' " *Reichhold Chemicals, Inc., supra,* at p. 64 of unreported slip opinion.

Conventionally Bonded Basic Bricks

The refractories industry, as far as this record shows, does not use the term "conventionally bonded basic brick." The industry does use the terms designated as the three main categories of that market: chemically bonded, regular burned, and direct bonded basic bricks (Finding 179) and recognizes this group of products as a distinct market. (Finding 200.) [55]

While rather cumbersome, the term "conventionally bonded basic bricks" does describe an area of effective competition where several refractories producers, including Lavino and Kaiser, were competing in 1973. These bricks vary substantially in price because of the different raw materials and methods by which they are made. (Findings 182-84.) But they all may be used in the same application. About half of the conventionally bonded basic bricks are sold to the steel industry where they are used in the linings of all steel-making furnaces except the BOF furnace. (Finding 192.) BOF bricks are not used interchangeably with conventionally bonded basic bricks (Finding 198), nor are nonbasic bricks. (Finding 199.) Conventionally bonded basic bricks are, however, used interchangeably with each other. Zoning practices depend on the characteristic degrees of cost and lining life of the three bricks, with chemically bonded being the least expensive and having the shortest life and direct bonded being the most expensive and durable. (Findings 183-85, 194.) Conventionally bonded basic bricks are also used in the production of cement, copper and glass, in the same parts of the kilns, furnaces and other equipment used to make those products. (Finding 193.)

Each of these types of bricks may be made on some production lines in a modern basic refractories plant. (Finding 186.) Shifting production of one type of conventionally bonded basic brick to another requires a change in raw material and a change in the temperature at which the bricks are treated. (Finding 187.) This takes but a few hours. (Finding 188.) Nonbasic bricks are not produced on the same production line as conventionally bonded basic bricks. (Finding 191.)

Respondent argues that other products should be considered in any market including conventionally bonded basic brick. These other products, however, cannot be made on the same production facilities and are much more expensive than most conventionally bonded basic bricks, or for other reasons should not be included in the relevant product market. For example, respondents argue that isostatically pressed bricks must be included. These bricks, however, are not even now produced in commercial quantities. (Sack, Tr. 406–07, 515; Garber, Tr. 903.) Chromic oxide bricks account for an infinitesimal percentage of basic brick sales. (CX 138A–F; CX 139G, I, K.) Rebonded fused grain and fused cast bricks are so expensive and have such high economies of scale that they are unique products not generally competing with conventionally [56] bonded basic bricks. (RX 499F; CX 139C; Ackerman, Tr. 1861–63, 1873–74, 1925; Findings 195–97.) That some of these products may be used instead of conventionally bonded basic bricks does not interfere with the relevant market finding. Like the plastic, paper and foil which could be used instead of glass and cans for containers in *Continental Can,* other competing products do not necessarily negate the existence of the submarket found here. 378 U.S. at 457–58. See also *United States* v. *Connecticut National Bank,* 418 U.S. 656, 663 n.3 (1974).

Respondent argues that different types of conventionally bonded basic bricks are not used interchangeably because they are used in different parts of steel-making furnaces.[20] Lack of cross-elastic demand, however, does not prevent different products from being included in a line of commerce if other factors are present. *Liggett & Myers Inc., supra,* at pp. 21,055–56 of Commission Opinion; *L. G. Balfour Co.* v. *FTC.* 442 F.2d 1, 10–11 (1972). Further, in *Sterling Drug, Inc.,* 80 F.T.C. 477, 593 (1972), the Commission pointed out that insofar as commonality of distribution is concerned, the important consideration is whether the products alleged to be in the same product market are sold through the same retail outlet—not where they are shelved within the store. Here, the important consideration is that all conventionally bonded basic bricks are used in steel furnaces (except BOF)—not where in the furnace present cost-benefit decisions place them.

[20] Zoning practices vary considerably from furnace to furnace in the steel industry. (Finding 30.)

Respondent stresses the differentiation of ingredients and characteristics of various refractories products, arguing that this prevents categorization for analysis of market effects. In *United States* v. *Continental Can Co., supra,* the Court grouped glass and metal containers—from different industries—in the same relevant product market. Those products have much greater physical differences than products found in the conventionally bonded brick market. See 378 U.S. 441, 445 n.3 and 446 n.4. Differences in price and qualities of shoes also did not interfere with the product markets found in *Brown Shoe Co.* v. *United States,* 370 U.S. 294 (1962). Here, because of industry recognition of the components of the market, common production facilities, distinct customers and vendors, and similar characteristics and uses, the three types of the conventionally bonded basic bricks constitute a relevant product market in which to test the effects of this acquisition. [57]

Geographic Market

The section of the country, for each of the product markets, in which to test the effects of this acquisition is clearly the United States. (Findings 86-93.) Respondent argues that one specialties product (dead burned dolomite) is sold regionally because of its low price and high transportation cost. But "the majority of products involved in this proceeding are distributed nationally and the major firms compete with others throughout the United States, a fact that compels finding that the nation as a whole constitutes the relevant market." *Beatrice Foods Co.,* 86 F.T.C. 1, 60 (1975), *aff'd,* 540 F.2d 303 (7th Cir. 1976). Furthermore, that freight costs are a significant factor and give an advantage to a seller with a plant located close to the customer does not foreclose firms from selling nationwide. *Ibid.*

Kaiser and Lavino and the refractories industry view the whole nation as their marketplace. (Findings 90-93.) In the few states where Kaiser and Lavino did not make sales to steel companies there were almost no customers for basic refractories. (Williams, Tr. 168-69; CX 168H-I.) But they sold wherever they could. (Findings 89-91) The geographic market determination must be made on the basis of where the parties could make sales as well as where they have made sales. *United States* v. *Bethlehem Steel Corp.,* 168 F. Supp. 576, 598 (S.D.N.Y. 1958).

The commercial realties established in this record indicate that the geographic market for basic refractories, and for each of the other product markets found herein, is national. *Jim Walter Corp.,* 90 F.T.C. 671, 747-53 (1977), appeal filed, Fifth Circuit Court of Appeals No. 78-1669.[21] [58]

Probable Effects on Competition

After determining the relevant markets, the next step is to ascertain whether the probable effects of the acquisition may be substantially to lessen competition in the markets. Statistics reflecting market shares and concentration are the primary index of this effect. *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 362-66 (1963). And where concentration in a market is already great, an acquisition which results in even small increases of market share will be presumptively unlawful. *United States* v. *General Dynamics,* 415 U.S. 486, 497 (1974).

Each of the relevant markets found herein was highly concentrated before the acquisition. (Findings 235-36, 238-39, 241-42, 244-45, 247-48.) After the acquisition, Kaiser was number two with 21 percent in basic refractories; number two with 18 percent in basic specialties; number two with 23 percent in basic bricks; number four with 12 percent in BOF bricks; and number two with 29 percent in conventionally bonded basic bricks. (Findings 236, 239, 242, 245, 248.) All of these markets were highly concentrated after the acquisition, with resulting four firm concentration ratios well over 60 percent. Horizontal acquisitions involving smaller market shares and concentration ratios have been proscribed under Section 7.[22] See cases collected in Commissioner Clanton's opinion in *Jim Walter Corp., supra,* 90 F.T.C. at pp. 756-59; *e.g., Beatrice Foods, Co.,* 86 F.T.C. 1 (1975), *aff'd,* 540 F.2d 303, 307 n.5 (7th Cir. 1976) where the acquiring and acquired firms had 7.6 and 2.3 percent of the brush and roller market, with a four firm concentration ratio rising from 41.3 percent to 43.6 percent; and *Warner Lambert Co.,* 87 F.T.C. 812, 880 (1976) where the combining firms had 4.4 and 4.2 percent of a market and the four firm concentration ratio increased from 45 to 48 percent. Here, in BOF bricks, the market in which the smallest market share was affected, the firm with 4 percent acquired the firm with 8

[21] Both exports and imports of basic refractories are relatively negligible and do not significantly change the analysis herein. (Williams, Tr. 358; CX 182Z5.) *United States* v. *Continental Can Co.,* 378 U.S. at 456-57. "[P]recision in detail is less important than the accuracy of the broad picture." *United States* v. *Brown Shoe Co., Inc.,* 370 U.S. 294, 342 n.69 (1962).

[22] Respondent relies on the Antitrust Division's Merger Guidelines, 1 CCH Trade Reg. Rep. ¶ 4510 at p. 6884, arguing that the effect on the BOF brick market involved less than the proscribed percentage. The acquisition here just missed the guideline total of 14 percent. Moreover, "[t]hese Guidelines are merely a public statement of intended allocation of prosecutorial resources . . . ." *Fruehauf Corp.,* 3 CCH Trade Reg. Rep. ¶ 21,402 (Feb. 22, 1978) at p. 21,371, appeal pending, Second Circuit Court of Appeals No. 78-4053. See also, *Stanley Works* v. *FTC,* 469 F.2d 498, 504 n.13 (2d Cir. 1972), *cert. denied,* 412 U.S. 928 (1973).

percent and the four firm concentration ratio went from 81 percent to 85 percent. [59]

With the statistical evidence involving market shares and concentration in markets found in this case, a rebuttable presumption shifts to the acquiring company the burden of proceeding to show that the market share statistics give an inaccurate account of the acquisitions' probable effects on competition. *United States* v. *Citizens & Southern National Banks,* 422 U.S. 86, 120 (1975); *United States* v. *General Dynamics Corp.,* 415 U.S. at 497 (1974).

Respondent's arguments fail to meet that burden. In 1973, Kaiser wanted more high kiln capacity since it was selling all the direct bonded basic bricks it could make, and the acquisition of Lavino gave it needed BOF brick capacity and plants closer to the eastern steel market. (Findings 74, 75.) Respondent Kaiser argues that the acquisition was procompetitive because it put Kaiser in a stronger position to compete against Harbison-Walker, the leader in refractories. This argument has been rejected as a matter of law by the courts. *Ford Motor Co.* v. *United States,* 405 U.S. 562, 569–70 (1972); *United States* v. *Bethlehem Steel Corp.,* 168 F. Supp. 575, 615–18 (S.D.N.Y. 1958).[23]

Respondent argues that only a minimal amount of money was involved in this direct competitive confrontation, and that in markets like BOF bricks neither Kaiser nor Lavino had been successful. But far smaller submarkets have been held substantial. *Seeburg Co.* v. *FTC,* 425 F.2d 124, 127 (6th Cir. 1970). And where two firms sell essentially the same product to the same types of customers, they are competing for Section 7 purposes, regardless of their success. *Id.* at 127–28; *American General Insurance Co.,* 89 F.T.C. 557, 630 (1977), appeal pending Ninth Circuit Court of Appeals No. 77-3207. Moreover, in the BOF market both Kaiser and Lavino were increasingly successful and were aggressively seeking new business. (Finding 178; CX 118N.) Therefore, their market share (Lavino at 8 percent and Kaiser at 4 percent) did not fully reflect the total impact on that market from the acquisition. *Cf. American General Insurance Co.,* 89 F.T.C. 557, 642 (1977). "Small but aggressive independents are the prototype of the firms Congress intended to preserve by enactment of Section 7." *Liggett & Myers, Inc.,* 87 F.T.C. 1074, 1181 (1976), *aff'd,* 567 F.2d 1273 (4th Cir. 1977). [60]

[23] Kaiser argues that the acquisition had procompetitive effects because Lavino allegedly was financially unstable. That argument is rejected, *infra,* at p. 63. Respondent also points to the testimony of competitors that the acquisition has not lessened competition. The opinions of Kaiser's competitors on the merits of the acquisition carry little weight. This testimony was evaluated in light of their "potentially hospitable attitude toward increased concentration and their interest in making similar acquisitions on their own." *American General Insurance Co.,* 89 F.T.C. 557, 663 (1977). (See Findigs 217, 218, 223.)

All of the markets involved in this case were concentrated. The *General Dynamics* case, *supra,* affirms the "importance of preventing even slight increases in concentration" in these markets. 415 U.S. at 497. Respondent argues that several professors of economics, including one of its witnesses, have the opinion that concentration is not an indication of oligopolistic behavior.[24] More important any such academic debate, however, is the dominant theme pervading congressional consideration of Section 7 which shows that the statute was meant by the legislators to stop the rising tide of concentration in the American economy. The Court stated in *Brown Shoe Co.* v. *United Sates,* 370 U.S. 294, 344 (1961) that it:

> cannot fail to recognize Congress' desire to promote competition through the protection of viable, small, locally owned businesses. Congress appreciated that occasional higher costs and prices might result from the maintenance of fragmented industries and markets. It resolved these competing considerations in favor of decentralization.[25]

The market shares and concentration ratios resulting from this acquisition show that little consideration need be given to "elaborate proof of market structure, market behavior or probable anticompetitive effects." *United States* v. *Philadelphia Nat'l. Bank,* 347 U.S. 321, 363 (1963). The record does contain evidence to show, however, that competition in the refractories industry will be lessened if this acquisition is allowed to stand. **[61]**

The basic refractories industry has very high barriers to entry including capital investment cost (Findings 206, 209), economies of scale (Finding 207), delay in entry time (Finding 208), and a technological barrier (Findings 209–12).[26] There have been no recent entrants and there were no potential entrants in 1973. (Findings 203–05.)

Historically there has been very little price competition in the basic refractories industry. (Findings 219–21.) This acquisition will decrease the chance of any price competition. (*E.g.,* Finding 223.) Before the Lavino acquisition, Kaiser viewed the merger trend in the refractories industry[27] as encouraging: "These mergers are viewed as a positive influence on industry ROA with anticipated emphasis on costs and prices." (CX 13J.) "Recent industry mergers will accelerate

[24] The traditional view of economists is well stated in F. Scherer, *Industrial Market Structure and Economic Performance,* (1971) at pp. 9, 13–19, 50, 183, 377, 466, 468.

[25] The acquisition also prevented the possibility of future deconcentration of the markets by Kaiser's internal expansion. Kaiser had the need and propensity. (Findings 43, 46, 47, 74, 75.) That loss is an unlawful effect in a horizontal merger case. *Stanley Works* v. *FTC,* 469 F.2d 498, 508 n.23 (2d Cir. 1972), *cert. denied,* 412 U.S. 928 (1973).

[26] High concentration may itself constitute a barrier to entry. *Fruehauf Corp.,* 3 CCH Trade Reg. Rep. ¶ 21,402 (February 22, 1978) at p. 21,366, appeal pending Second Circuit Court of Appeals No. 78-4053.

[27] Kaiser also has a history of growing in the refractories industry by acquisition. (Finding 41.)

price firming as evidenced by Harbison-Walker leadership." (CX 13K.)[28] In 1973, while Kaiser executives contemplated the acquisition of Lavino, they speculated that: ". . . [W]ith the anticipated reduction in the number of supplies, it is expected generally that the direct bonded pricing will strengthen rather than erode." (CX 101B.)[29] And, while Kaiser now argues that Lavino was financially weakened before the acquisition, the Kaiser Refractories Strategic Plan for 1973–82 asserted that price competition which occured in the refractories industry was caused by just such "financially weaker companies exerting a downward force from published book prices." (CX 56Q.) **[62]**

The oligopolistic behavior of the basic refractories industry is also indicated by a Kaiser document which stated that its (CX 13Q):

> Current R&D philosophy is not to interrupt a product life cycle by innovating its obsolescence. In some instances, the tendency is to react to competition rather than customer needs. . . . The cost of taking innovative leadership from Harbison-Walker is unknown and the benefits are questionable.

In this concentrated, oligopolistic industry, the effect of allowing the acquisition to stand would be to encourage even further concentration "by triggering other mergers by companies seeking the same competitive advantages sought by [Kaiser] in this case." *Unites States* v. *Continental Can Co.*, 378 U.S. 441, 464 (1964). Other basic refractories producers are watching this case, with the intent to merge if possible. (Finding 223.) For example, in August of 1975, Martin-Marietta, a leading basic specialties producer, saw the increased prices and profits in the production of basic direct bond and BOF bricks and studied the acquisition of a basic brick manufacturer. (CX 213Z11–Z13.) Their market plan advised against building new basic brick production facilities because (RX 474Z12): "This is time consuming and adds another brick supplier to share the market." Also, North American Refractory Company acquired the fifteenth largest basic refractories company in 1977 and is looking for additional mergers. (Finding 223.)[30]

Before the acquisition, Kaiser and Lavino were direct, substantial competitors in each of the markets found herein. (Findings 114, 134, 178, 201, 224–33.) The acquisition eliminated that substantial competition. There is no doubt that this acquisition had anticompetitive effects on the markets for basic refractories products. **[63]**

General Dynamics

In *United States* v. *General Dynamics Corp.*, 415 U.S. 486 (1974), the Court looked at the history and probable future of the market and found no probable anticompetitive effects resulting from a horizontal merger of two companies mining coal. The Court found

[28] In basic bricks, Harbison-Walker "has either adopted or been delegated the role of pricing leadership." (CX 214 C–D.)

[29] Kaiser's prediction was correct. Prices for basic direct bond and BOF bricks increased in 1974 from $230 to

the "focus of competition" in the coal industry to be the procurement of long term supply contracts. The acquired company's coal reserves were almost totally committed and it had no possibility of acquiring more. 415 U.S. at 503. Since the acquired company could not compete in the future, the merger could not substantially lessen competition.

Relying on *General Dynamics,* respondent argues that Lavino was competitively weak prior to the acquisition and in the future would not have been a "viable competitive factor in the industry." In making this argument, respondent bears a heavy burden. *United States* v. *Amax, Inc.,* 402 F. Supp. 956, 970 n.53 (D. Conn. 1975). Respondent must show, as a matter of law, that Lavino "lacked the wherewithal to compete" in all of its markets. *Id.* at 970-71. Mere financial weakness (unless it amounted to a "failing company" defense) is not the test.[31] The fact that it may not have been Lavino itself which would have continued competing in the future is irrelevant. *Id.* at 971. Unless respondent can prove that it was improbable that the Lavino basic refractories plants could have stayed in business, the defense must fail. Lavino's competitive weaknesses were not a defense. [**64**] "There is no such quasi-failing company defense available under Section 7 of the Clayton Act." *Reichhold Chemicals, Inc., supra,* at p. 72 of slip opinion.[32]

Even if such a defense existed, respondent's factual arguments have no merit. Respondent argues that, but for the acquisition, Lavino eventually would have been liquidated.[33] [**65**] This argument fails for lack of proof. Respondent's exhibit (RX 478) and witnesses offered to support this theory were unreliable, speculative and inconsistent.[34] Furthermore, where the acquired company was a division of a large profitable company like IMC, the financial records

[31] Respondent did not raise the "failing company" defense which has been narrowly construed. *Citizen Publishing Co.* v. *United States,* 394 U.S. 131, 136-39 (1969). *Reichhold Chemicals, Inc., supra,* pp. 71-72 n.92.

[32] Other cases hold that *General Dynamics* calls for an assessment of the probable future health of the acquired company as if the acquisition had not occured. *United States* v. *Consolidated Foods Corp.,* 1978-1 Trade Cases ¶ 62,063 (E.D. Pa. 1978), appeal filed July 10, 1978, allowed the defense where technological difficulties and limited product variety caused the acquired company's declining sales and "impaired its ability to compete in the future." *Id.* at p. 74,614 n.19.

In *Pillsbury Co.,* Dkt. 9091 [93 F.T.C. ——] (Initial Decision by Administrative Law Judge Joseph Dufresne, May 15, 1978), appeal pending, the defense was applied in an intensely competitive industry dominated by large firms and the acquired company was financially weak, had production problems, required capital, could not offer needed advertising assistance and other promotions, and had a debilitated division. *Id.* at p. 59.

United States v. *International Harvester Co.,* 564 F.2d 769 (7th Cir. 1977), would extend the *General Dynamics* test to require the assessment of whether the "weakened" or "very precarious" financial condition of the acquired company would leave it "sufficient resources to compete effectively." This test, with its balancing of books, weighing of debt-equity ratios, allocations of costs, and "Z-scores" (Thorne, Tr. 3154-68), is highly speculative. "There is nothing, however, in *General Dynamics* which says that fluctuations in prices, costs, or profits are to be weighed routinely in Section 7 cases as countervailing factors which may distinguish the effects of a permanent structural change brought about by the acquisition." *Reichhold Chemicals, Inc., supra,* slip opinion at 70-71.

[33] Even if the competitive health of Lavino at the time of the acquisition were relevant, respondent would have to show *imminent* competitive disability. An argument that Lavino might be liquidated eventually would amount to "uncabined speculation." *Cf. BOC International Ltd.* v. *FTC,* 557 F.2d 24, 28-30 (2d Cir. 1977).

[34] See citations to the record by complaint counsel in their reply brief pp. 4-8, 79-81.

of the parent must be part of such a defense. *Farm Journal, Inc.*, 53 F.T.C. 26, 47–48 (1956); *Calnetics Corp.* v. *Volkswagen of America, Inc.*, 348 F. Supp. 606, 622 (C.D. Cal. 1972).[35]

Respondent argues that Lavino's share of the basic refractories market had declined and that further decline was inevitable.[36] In fact, Lavino's market share from 1969 to 1973 was relatively stable. (RPF 410, *in camera*.) Its share of the dynamic BOF brick market doubled during that period and it was stepping up its marketing efforts and was increasingly successful. (Findings 68, 174, 178; RPF 397, *in camera;* Burriss, Tr. 1470.) And Kaiser knew that the market for Lavino's direct bonded bricks was growing. (Finding 74; CX 149D.) Lavino's dominance in direct bonded bricks and growing vigor in BOF bricks probably would have resulted in increased sales and profits. In August of 1975, [66] Martin-Marietta, a leader in the production of basic specialties but not a producer of basic bricks, saw growth potential in the production of basic direct bond and BOF bricks (RX 474Z11); "The price structure of Basic Direct Bonded and BOF Bricks increased three times last year from $230 up to $350 per ton average selling price. This significant price increase makes brick manufacturing far more attractive than in our previous studies."

Although at the time of acquisition Lavino was no longer integrated vertically into the production of magnesia, this was not necessarily a competitive disadvantage. Because of the oversupply of magnesia, some basic refractories producers prefer to shop for a supplier rather than produce their own material. (Williams, Tr. 174–75; Seelig, Tr. 2152–53.)

Kaiser argues that IMC's cutbacks on research and development weakened Lavino. However, at the time of the acquisition, Lavino's R&D had a reputation as one of the top in the industry. (Williams, Tr. 196; Hall, Tr. 2298–99.) And Kaiser must have thought Lavino's R&D staff was competent. After the acquisition, Kaiser replaced its own basic refractories R&D staff with the Lavino personnel. (Finding 82.)

Respondent also argues that IMC had withheld necessary capital from Lavino, putting it in a weakened position. While the record shows that IMC had a cost cutting policy (Findings 59, 60), and

[35] The books of a division can easily be adjusted by the parent, through allocations of debt, interest and other overhead costs, to make the division appear less profitable than it is. (Thorn, Tr. 3342–43; Rowe, Tr. 3902–03, 3980–90.) The accounting standards of the parent should not be used to determine whether its division is failing financially. *Cf. Reichhold Chemicals, Inc., supra*, at pp. 72–73.

[36] This prediction is based in part on the assumption that Lavino was a narrow line, high cost producer. Lavino was, in fact, a broad line basic refractories producer. (Finding 225.) There are few advantages in producing both basic and nonbasic refractories. (Findings 104, 105, 113, 140.) Lavino's costs did not stop it from being profitable. (Finding 72.) And Kaiser knew those costs when it made the acquisition. (Findings 76, 79.)

Lavino's plants did have EPA and OSHA problems, and quality control and delivery problems at the time of the acquisition,[37] Lavino remained an effective competitor, accounting for a substantial share of each product market. (Findings 236, 239, 242, 245 and 248.)[38] There is no proof that Lavino's need for capital improvements at its plants was uncommon (Adams, Tr. 247) and these problems did not dissuade Kaiser from making the acquisition. Even with these expenditures, Kaiser planned that its profits from the Lavino plants would double its normal rate of return. (CX 66D.) [67]

REMEDY

This acquisition is "patently illegal and indefensible, and respondent must bend every effort" to restore Lavino as a viable competitor. *Reichhold Chemicals, Inc., supra,* at p. 73; see also *Ford Motor Co.* v. *United States,* 405 U.S. 562, 572–78 (1972); *Ekco Products Co.,* 65 F.T.C. 1163, 1212–17 (1964), *aff'd,* 347 F.2d 745 (7th Cir. 1965). Only complete divesture, including divesture of after-acquired assets, can return Lavino to a position which assures another competitive force offering alternatives to buyers in the highly concentrated and oligopolistic basic refractories industry. *Fruehauf Corp., Inc., supra,* 3 CCH Trade Cases at pp. 21,377–79; *Liggett & Myers, Inc., supra,* Initial Decision, 87 F.T.C. at p. 1140; "In the absence of proof to the contrary the assumption of this Commission must be that 'only divestiture can reasonably be expected to restore competition and make the affected markets whole again.' " *Diamond Alkali Co.,* 72 F.T.C. 700, 742 (1967), quoting from *National Tea Co.,* 69 F.T.C. 226 (1966).[39]

The order also prohibits Kaiser from acquiring another basic refractory producer for fifteen years without Federal Trade Commission approval. Kaiser has a history of acquiring basic refractories producers. The industry has had no recent entrants; has no potential entrants and high entry barriers; and is highly concentrated and subject to oligopolistic behavior. While not amounting to the monopolistic practices providing the basis for a twenty year prohibition, *Ekco Products Co.,* 65 F.T.C. 1163, 1217, 1228 n.3 (1964), *aff'd*

[37] Kaiser and other major refractories producers also had similar problems. (Mittsoff, Tr. 1776, 1779, *in camera;* Adams, Tr. 2471.)

[38] Lavino's efforts in the BOF market (Findings 174, 178), the loyalty it had developed for its products in the steel industry (Findings 212, 228) and its established distribution system, all implied future competitive strength which overcomes the *General Dynamics* defense. *American General Insurance Co., supra,* 89 F.T.C. at 642.

[39] The order requires ancillary relief appropriate to correct the effects of anticompetitive practices engaged in by respondent. None of the provisions, however, involve novel and major relief such as that involved in *Liggett & Myers, Inc., supra,* 87 F.T.C. at 1182, which might merit additional argument or evidence. Moreover, any comments by the parties on these provisions may be filed with the Commission which has the authority to issue a final order herein.

347 F.2d 745 (7th Cir. 1965), the facts here require a longer acquisition ban than in previous merger cases where a ten year ban was sufficient. *Jim Walter Corp., supra,* 90 F.T.C. 671 (1977).

Respondent urges that only one of the plants should be divested, but with the relatively high economies of scale in this industry such a divesture might not create a viable competitor. And, since the Gary plant and the Plymouth Meeting plant make different products, the new competitor will have a broad line, which will help it to compete against the major basic refractories producers. [68]

A spin-off of the divested entity might create an independent competitive force which the basic refractories industry certainly needs. There is the possibility, however, that the purchase of the Lavino business by a large company not previously in the basic refractories business would expedite its resuscitation. *Jim Walter Corp., supra,* 90 F.T.C. at 765.

Respondent urges that it should not be required to sell the Lavino business at a price lower than its liquidation value. That is a matter which can best be determined after some effort is made to comply with this order. But in no event should the sale price allow respondent to profit from the possible appreciation in the value of the assets involved. *Reichhold Chemicals, Inc., supra,* at pp. 73–74. The price should not exceed the amount paid by Kaiser plus the actual cost of subsequent improvements.

The order will require that any improvement in the Lavino business made by respondent since the acquisition shall be divested. The record shows that this occurred in part to meet government health and safety standards and for pollution control. This equipment should be included as part of the Lavino business to be divested. The Commission may properly require that the acquired firm be recreated in a form which will reflect the firm's probable growth, including improvements it may have added itself. *United States* v. *Aluminum Co. of America,* 247 F. Supp. 308, 316 (E.D. Mo. 1964), *aff'd mem.,* 382 U.S. 12 (1965) (order required divestiture of a plant built after unlawful acquisition); *Union Carbide Corp., supra,* 59 F.T.C. at 657, 673 (divestiture of all of the post-acquisition improvements and equipment installed on premises of acquired company); see generally Elzinga, *The Antimerger Law: Pyrrhic Victories,* 12 *Journal of L. & Econ.* 43 (1969).

The order will provide the purchaser of the Lavino business with an assured source of supply of magnesia, the primary raw material for basic refractories. One of the most important assets acquired by Kaiser was Lavino's long term supply contract with Harbison-Walker for magnesia. Kaiser would not have made the acquisition without that contract, and took advantage of the option to renew it. In an attempt to put the Lavino business back in the shape it would have been in but for the acquisition, the order will therefore provide that Kaiser (which has a magnesia supply for its own use) will supply equivalent grades, amounts and prices for the magnesia which will be needed by the purchaser of the Lavino business to penetrate the market again. See *United States* v. *Kennecott Copper Corp.*, 249 F. Supp. 154, 162 (S.D.N.Y.), *aff'd mem.*, 381 U.S. 414 (1965); *cf. Ford Motor Co.* v. *United States*, *supra*, 405 U.S. at 572. **[69]**

The order will also require Kaiser to supply to the purchaser know-how developed by Lavino and by the Lavino research and development personnel who now staff Kaiser's basic refractories R&D division. *Reichhold Chemicals, Inc., supra*, at p. 75. The Order does not punish Kaiser by requiring it to turn over know-how which it developed on its own prior to the acquisition.

The order also requires Kaiser to help put the Lavino business in a position where it can sell what it makes. After the acquisition, Kaiser fired most of the Lavino sales personnel. The order therefore requires Kaiser to help find and train sales personnel, to provide them with customer lists, and to cease soliciting, for a time, the customers obtained from Lavino. Since both Lavino and Kaiser sold to some of the same customers prior to the acquisition, the order applies only to the customers who bought from Lavino and not from Kaiser.[40] These provisions are designed " 'to give the divested [company] an opportunity to establish its competitive position' and the time it needs to 'obtain a foothold in the industry.' " *Reichhold Chemicals, Inc., supra*, at 75, quoting *Ford Motor Co.* v. *United States*, 405 U.S. at 575. **[70]**

Conclusions of Law

1. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and over respondent Kaiser.

2. On February 28, 1974, Kaiser acquired two basic refractory plants and related assets from International Minerals & Chemical Corporation (IMC). These assets were part of the Lavino Division of IMC.

3. At all times relevant to this proceeding Kaiser and IMC and Lavino were engaged in commerce within the meaning of the Clayton Act and the Federal Trade Commission Act.

[40] The term "customer facility," rather than "customer," is used in the order. The decision as to which basic refractories company to buy from is made at each plant. (Findings 113, 178; CX 114H) For example, both Kaiser and Lavino sold BOF products in 1971 to the Wheeling-Pittsburgh Steel Corp. plant in Monessen, Pennsylvania. But at that steel producer's Steubenville, Pennsylvania, plant, Lavino was a supplier and Kaiser was not. The order would therefore prohibit Kaiser from soliciting the Steubenville plant.

4. For the purpose of assessing the legality of the acquisition the relevant lines of commerce are the manufacture and sale of: (i) basic refractories; (ii) basic refractory specialties; (iii) basic refractory bricks; (iv) basic oxygen furnace bricks; and (v) conventionally bonded basic bricks.

5. The United States as a whole is an appropriate section of the country within which to test the effects of the acquisition.

6. Prior to, and at the time of the acquisition, Kaiser and IMC's Lavino Division were actual competitors in the United States in each line of commerce set out in Conclusion #4.

7. The acquisition eliminated substantial actual competition between Kaiser and IMC's Lavino Division and between IMC's Lavino Division and other firms in each line of commerce set out in Conclusion #4.

8. The acquisition substantially increased concentration and decreased the possibility of deconcentration in each line of commerce set out in Conclusion #4.

9. Additional acquisitions and mergers in each line of commerce set out in Conclusion #4 may be encouraged if this acquisition were permitted.

10. The acquisition raised the already high entry barriers in each line of commerce set out in Conclusion #4.

11. The acquisition strengthened the position of Kaiser in each line of commerce set out in Conclusion #4. [71]

12. The effect of the acquisition of Lavino by Kaiser may be substantially to lessen competition in each line of commerce set out in Conclusion #4 in the United States, in violation of Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act.[41]

13. Divestiture, including all improvements and all after acquired property, is both necessary and appropriate to remedy the anticompetitive effects of this unlawful acquisition. In addition, Kaiser should be required to provide technical assistance, marketing assistance and raw materials to the purchaser of the divested Lavino assets. Finally, Kaiser should be prohibited from acquiring any basic refractory producer, without prior approval of the Federal Trade Commission, for a period of fifteen (15) years. [72]

Order

I

It is ordered That:

[41] No separate proof or arguments were made under the Section 5 count but any violation of Section 7 is a violation of Section 5. *FTC* v. *Brown Shoe Co.*, 384 U.S. 316, 321–22 (1966).

Respondent Kaiser Aluminum and Chemical Corporation (hereinafter "Kaiser"), a corporation, and its officers, directors, agents, representatives, employees, subsidiaries, affiliates, successors, and assigns, shall divest all assets, title, properties, interests, rights and privileges of whatever nature, tangible, and intangible, including without limitation all real property, buildings, machinery, equipment, tools, raw materials reserves, inventory, customer lists, trade names, patents, trademarks and other property of whatever description acquired by Kaiser as a result of its acquisition of the basic refractories segment of the Lavino Division of International Minerals and Chemical Corporation (hereinafter "Lavino" and "IMC") together with all additions and improvements to said property which have been made subsequent to the acquisition. Such divestiture shall be absolute, shall be accomplished no later than one year from the effective date of this order, and shall be subject to the prior approval of the Federal Trade Commission. [73]

II

Within 20 days of the effective date of this order, pending divestiture, the property and business specified in Paragraph I shall be maintained and operated as a separate corporation with separate books and accounts, separate management, separate assets, and separate personnel.

III

Pending divestiture, no substantial property or other assets of the separate corporation referred to in Paragraph II herein shall be sold, leased, otherwise disposed of or encumbered, other than in the normal course of business, without the consent of the Federal Trade Commission, and Kaiser shall not commingle any assets owned or controlled by such separate corporation with any assets owned or controlled by Kaiser.

IV

For the period of three years from the date on which this order becomes final, no individual employed by the separate corporation referred to in Paragraph II herein shall be hired by Kaiser. [74]

V

Pending divestiture, Kaiser shall maintain the separate corporation referred to in Paragraph II herein as an independent entity and take no steps to impair such corporation's economic and financial position.

VI

Pending any divestiture required by this order, Kaiser shall not allow the deterioration of the property specified in Paragraph I in a manner that impairs the marketability of the business.

VII

Pursuant to the requirements of Paragraph I, none of the property or business acquired or added by Kaiser shall be divested to anyone who is an officer, director, employee or agent of Kaiser or is in any other way controlled or influenced by Kaiser, or to anyone who owns or controls, directly or indirectly, more than one percent of the outstanding shares of the capital stock of Kaiser or to anyone who is not approved in advance by the Federal Trade Commission. [75]

VIII

For a period of fifteen years from the date this order becomes final, Kaiser shall cease and desist from acquiring or acquiring and holding directly or indirectly, through subsidiaries or otherwise, without the prior approval of the Federal Trade Commission, the whole or any part of the stock, share capital or assets, or any other interest in any company engaged in the business of manufacturing, distributing, or selling basic refractories.

IX

For a period of five years from the date of the divestiture specified in Paragraph I, Kaiser shall provide upon request of the purchaser, without charge, the use of all know-how, patents, and trade secrets developed by the Kaiser Refractories Division basic refractories research and development staff since the acquisition by Kaiser of the Lavino assets.

X

For a period of three years from the date of the divestiture described in Paragraph I, if requested by the purchaser for its own use, Kaiser shall provide such amounts and grades of magnesia as are requested, with the maximum amounts, grades and prices to the purchaser limited to that received by Kaiser under the supply contract (or any renewal pursuant thereto) obtained by Kaiser from

Harbison-Walker in the acquisition [76] of the Lavino assets. Kaiser shall provide the purchaser reasonable access to documents sufficient to allow the purchaser to determine whether Kaiser is in compliance with the provisions of this paragraph.

XI

For a period of one year from the date of the divestiture described in Paragraph I, Kaiser shall, if requested by the purchaser, without charge, in good faith, assist the purchaser in hiring and training a staff for research and development and for sales of basic refractories. Kaiser shall, in this regard, pay the expense of obtaining, through an employment agency picked by the purchaser, competent, technically trained, basic refractories salesmen and research and development scientists, and their supervisors. The number of such personnel shall not exceed the number employed by Lavino on November 9, 1973.

XII

At the time of the divestiture required by this order, Kaiser shall make available to the purchaser of the property and business, a list of all of Kaiser's customers for basic refractories products who have purchased said products from respondent within three years prior to the divestiture. [77]

XIII

For a period of two years from the date of the divestiture described in Paragraph I, Kaiser shall not solicit, for the purpose of selling basic refractories products, any customer facility which purchased said products from Lavino, and not from Kaiser, during the year prior to the acquisition.

XIV

Any dispute arising under Paragraph IX through XIII of this order shall be resolved at the option of either Kaiser or the purchaser pursuant to the Commercial Arbitration Rules and the procedures of the American Arbitration Association. If arbitration is invoked by either party, such arbitration shall be exclusive and in lieu of any other common law rights. The arbitrator shall be selected by the parties from the panel of arbitrators of the American Arbitration Association or by the Federal Trade Commission in the event that the parties are unable to agree; said arbitrator shall be empowered to determine the merits of any dispute arising under Paragraphs IX through XIII of this order, and assess the costs of arbitration; the

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decision of said arbitrator shall be final and binding upon the parties and judgment thereon may be entered in any court of competent jurisdiction. Arbitration shall be no cause for delay; and in the event of a default by either party in appearing before the arbitrator, pursuant to advance written notice, the arbitrator is authorized to render a decision upon the testimony of the party appearing. [78]

XV

One year from the effective date of this order, and on the anniversary date of each year thereafter until the expiration of the prohibitions in Paragraph VIII of this order, Kaiser shall submit a report in writing to the Federal Trade Commission listing all acquisitions, mergers and agreements to acquire or merge made by Kaiser relating in any way to the production or sale of basic refractories; the date of each such acquisition, merger or agreement; the products involved and such additional information as may from time to time be required.

XVI

Within thirty days from the effective date of this order and every sixty days thereafter until it has fully complied with Paragraph I of this order, Kaiser shall submit a verified report in writing to the Federal Trade Commission setting forth in detail the manner and form in which it intends to comply, is complying or has complied therewith. All such reports shall include in addition to such other information and documentation as may hereafter be requested: (a) a specification of the steps taken by Kaiser to make public its desire to divest Lavino, (b) a list of all persons or organizations to whom notice of divestiture has been given, (c) a summary of all discussions and negotiations together with the identity and address of all interested persons or organizations, and (d) copies of all reports, internal memoranda, [79] offers, counteroffers, communications and correspondence concerning said divestiture.

XVII

Kaiser shall notify the Commission at least thirty days prior to any proposed changes by it which may affect compliance obligations arising out of this order.

OPINION OF THE COMMISSION

BY DIXON, *Commissioner:*

On February 28, 1974, respondent Kaiser Aluminum & Chemical Corporation acquired two refractory plants and the related assets of the Lavino Division of International Minerals & Chemical Corporation. Complaint issued on April 27, 1976, charging that the acquisition violated Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act.

Both Kaiser, a diversified company doing business internationally and one of the United States' largest corporations, and Lavino were, at the time of the acquisition, engaged in the manufacture and sale of refractories throughout the United States. The complaint alleged that in the five relevant product markets[1] the acquisition eliminated substantial competition between Kaiser and Lavino, increased already high levels of concentration, raised barriers to entry, will increase concentration by precipitating additional acquisitions, and strengthened Kaiser's competitive position. [2]

Hearings were held before Administrative Law Judge James Timony, who filed an initial decision on October 13, 1978, concluding that the acquisition violated Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act and recommending an order requiring Kaiser to divest the Lavino assets. The ALJ's holding that the acquisition was illegal was based principally upon the findings that there were, as alleged, five relevant product markets; that in each concentration was high (among the top four firms, it ranged from 62.16% to 85.44%); and that concentration increased significantly in each of the markets as a consequence of the acquisition (among the top four firms from 3.13% to 10.5%). The matter is before the Commission on the appeal of respondent from the initial decision.

A. The Products

Refractories are materials that line furnaces and reactors and are designed to withstand the intense heat necessary to "smelt ores, refine materials, generate steam power and to produce glass, Portland cement, pottery and building brick". (CX 178 "O")[2]

All refractories have in common the capacity "to allow a useful or desirable process or event to be controlled at temperatures above a dull red heat". (CX 232J) More specifically, refractories must remain

[1] On September 8, 1976, the complaint was amended, adding two product markets to the original three.

[2] The following abbreviation are used herein:

I.D.	- Initial Decision
I.D. p.	- Initial Decision, Page No.
CX	- Complaint Counsel's Exhibit No.
RX	- Respondent's Exhibit No.
Tr.	- Transcript of Testimony, Page No.
RAB	- Respondent's Appeal Brief

stable at high temperatures and must withstand pressures from the weight of the furnace parts or contents, the thermal shock resulting from rapid heating or cooling, other stresses induced by temperature change, mechanical wear resulting from movement of furnace contents and chemical attack by heated solids, liquids, gases or fumes. (CX 232J) [3]

Refractories are classified by (a) their composition, (b) shape, (c) the method by which their mechanical strength is imparted, and (d) their resistance to chemical attacks.

Refractory Composition

The raw materials used to construct refractories are magnesia, chrome ore, dolomite, fire clay, silica and alumina.

Refractory Shapes

Refractories are generally pre-formed, most commonly into a 9" x 4-1/2" x 2-1/2" shape. To meet special needs, some refractories are pre-formed in such shapes as arches or wedges. All pre-formed refractories are referred to as "bricks." Refractories that are unformed are referred to as "specialties" and include ramming and casting mixes, cements and mortars, and furnace grains. (CX 95Z-91)

Imparting Strength

Refractory bricks obtain their strength through exposure to fire, chemicals or tar. A brick subjected to a relatively low temperature fire is known as a "regular burned brick," while one subjected to a higher temperature fire is a "direct bonded brick." When a brick is bonded by chemicals such as epsom salts, the industry calls it a "chemically bonded brick." When tar is added to the brick during mixing, it is known as a "tar bonded brick." A brick saturated with tar after it is fired is called a "tar impregnated brick." (CX 95Z-85; CX 111G-H)

Resistance to Chemical Attack

Refractories are either basic or non-basic depending upon their capacity to resist chemical or acid erosion. As expressed by Kaiser in its "Handbook of Refractory Products" (CX 95Z-73), "Chemically speaking, refractories may be divided into two major groups—acid and basic. Basic refractories, alkaline [unacid] in nature, are made from . . . magnesia, and chrome ore" and, as such, resist chemical emissions. In direct contrast, non-basic refractories are designed to withstand acid emissions. [4]

It should by now be evident to the bewildered reader that because a refractory may be made of one or more of six raw materials and because the proportion of the raw material or raw materials will give it distinct performance characteristics as will the method of bonding and its shape, a wide variety of refractories are produced. By combining different bonding processes and raw material mixes, the industry produces, for example, direct bonded magnesia/chrome bricks, tar bonded carbon/magnesia bricks, tar-impregnated magnesia bricks, tar bonded magnesia bricks, chemically bonded chrome/magnesia bricks, regular burned magnesia/chrome bricks, and direct bonded magnesia/chrome bricks.

Uses of Refractories

In a typical furnace or reactor, a wide variety of refractories may be deployed, since the demands placed upon the refractory vary with its location in the furnace. By way of illustration, in a publication entitled *Refractories for the Direct-Arc Electric Furnace Basic Slag Practice* (CX 254), the refractory manufacturer, A.P. Green, discusses refractory needs in each section of the electric arc furnace. As an example, A.P. Green examines the requirements in the furnace's subhearth and lower side walls, noting that refractories placed there must be capable of containing molten steel. A magnesia refractory brick is recommended because it is "an excellent contact material for this use, since it has a very high melting point . . . and goes into solution in lime rich slags very slowly . . . A burned, high purity hydration resistant magnesia brick . . . is normally recommended for this area . . . . To lower the initial cost, some operators prefer magnesite brick . . ., chrome-magnesite brick . . ., or even fire claybrick beneath a top layer of burned magnesia brick. Since subhearths are generally not replaced for many furnace campaigns, the economy of compromising on quality in this area is questionable." (CX 254F)

The company, in examining that portion of the electric arc furnace called "the working hearth," notes that the use of fire clay bricks (a non-basic refractory) makes for rapid erosion. So instead, "the bottoms of most basic . . . electric arc furnaces are constructed of a high purity of magnesia ramming mix . . . Burned magnesia brick . . . bottoms are used from time to time with excellent success. Some use is also being made of vibrated high purity dolomite." (CX 254"O") [5]

At the slag line, A.P. Green goes on to point out, a high purity burned magnesia brick has historically been recommended. "Some 15 years ago fused basic brick . . . became available, and these products do an excellent job of resisting chemical solution. However, they are expensive, costing several times as much as [high purity magnesia brick], and they are difficult to patch because nothing will fuse to them. More recently three new types of brick have further application in slag lines: direct bonded magnesia-chrome . . . . rebonded fused grain brick; and high fired burned magnesia impregnated with pitch . . . ." Of these, the magnesia-chrome brick and the fused grain brick were more tolerant of slags that "move over onto the acid side at times", while the magnesia impregnated with pitch brick was "superior to these in resistance to chemical solution in strongly basic slags high in lime and iron oxide. The pitch impregnation . . . gives it superior resistance to slag penetration." (CX 254W)

B. The Companies

Kaiser, a Delaware corporation, is a fully integrated aluminum producer engaged in the production of agricultural chemicals, industrial chemicals and refractory materials. With revenues in 1973 totalling $1.28 billion, *Fortune* magazine ranked it as the 133rd largest corporation and with assets of $1.81 billion, as the 67th largest firm. Its net income in 1973, before extraordinary items, was $44.54 million. Kaiser, which supplies refractories to producers of iron and steel, glass, cement, petroleum, chemicals and copper, entered the refractory business in 1943 with the opening of a plant at Milpitas, California. In later years it added refractory plants at Natividad and Moss Landing, California. To expand its sales to major steel producers, Kaiser constructed in 1956 a basic refractories plant at Columbiana, Ohio. The company first installed high temperature kilns at its Moss Landing facility in the mid 1960's and to accommodate unusual demand for direct bonded bricks, constructed an additional kiln in 1973. By the late 1960's Kaiser was producing BOF (basic oxygen furnace) bricks in its Columbiana plant. Sales of tar bonded bricks reached $1.6 million in 1973. Up to the time of the challenged acquisition, Kaiser operated its refractory business at a profit. [6]

Lavino, which was founded in 1887, first produced basic refractories after World War I at a plant in Plymouth Meeting, Pennsylvania. In the early 1950's, a facility for the construction of refractories was built at Newark, California. A plant producing raw materials was established at Freeport, Texas, in 1960. In that same year, a basic refractory plant was constructed at Gary, Indiana, for the purpose of supplying steel producers. The company added a tar bonding facility to its Gary plant in 1963 when it entered the BOF refractories business.

Lavino was responsible for a number of innovations in the refractories industry. In 1962, it produced the first direct bonded basic refractory brick. In earlier years, it was first to produce plastic chrome ore and fosterite bonded chrome/magnesia brick, and to use chrome ore supplied from a variety of different countries. In 1966, Lavino was purchased by International Minerals & Chemicals Corporation (IMC) for approximately $26 million. IMC is a highly-diversified, industrial corporation, which in 1973 showed total sales of $555.86 million; net earnings before income taxes and extraordinary items of $36.14 million, and total assets of $259.89 million. In January, 1971, IMC initiated several changes in the Lavino operation, transferring officers and employees, making public its desire to sell the company, limiting expenditures to the maintenance of the daily operation of the business, and closing Lavino's Newark plant. A year later, in 1972, Lavino's Freeport magnesia plant and its Newark production facility were closed. While expenditures in research and development were cut from $636,000 in fiscal 1971 to $532,000 in 1972 and then to $404,000 in the fiscal year 1973, Lavino did not reduce its professional R&D staff. The cutbacks were achieved by reducing expenditures in other areas, including new testing equipment. Lavino's earnings in 1968–69 were $3,433,000; in 1969–70, $2,873,000; in 1970–71, $17,000; in 1972–73, $2,380,000; and in the first half of 1973–74, $1,779,000. During fiscal year 1971–72, when steel production dipped sharply, Lavino realized a loss of $340,000.

C. Relevant Markets

The administrative law judge found that the "section of the country" or geographic market in which the merging parties competed was the United States as a whole, a finding that neither side contests and one that is clearly established by the record. Respondent, however, objects strenuously to the ALJ's determination of relevant product markets. [7]

The Overall Market: Basic Refractories

In considering whether a diverse number of products such as those that comprise the basic refractory market constitute a relevant line of commerce, we must not include an "infinite range" of products, *Times-Picayune* v. *United States,* 345 U.S. 594, 612 n.31 (1953), nor insist that the products "be fungible," *United States* v. *duPont,* 351 U.S. 377, 394 (1956). As the Court admonished in *United States* v.

Continental Can Co., 378 U.S. 441 (1964), it is necessary to look between these two extremes and "recognize meaningful competition where it is found to exist." 378 U.S. at 449. Guideposts to the recognition of markets, such as the reasonable interchangeability of end use of the various products, cross-elasticity of production facilities and the *Brown Shoe*[3] criteria for submarkets may be discerned only by "a careful consideration based upon the entire record."[4] We have examined the record with particular emphasis on two factors: interchangeability of end use and cross-elasticity of production.

Interchangeability of End Use

At least 80% of basic refractory production is used in steelmaking, and thus patterns of refractory use in steelmaking are most relevant in determining the degree of interchangeability among various refractories. In each of the steelmaking furnaces, open hearth, electric arc, argon oxygen decarburization[5] and basic oxygen, the type of refractory (its shape, its bond and the raw material) to be deployed in a given location is determined by a practice known as "zoning". Each furnace is divided into wear areas or zones. Refractories of the highest quality are used in the highest wear areas, those of the lowest quality in the lowest wear areas. In this way wear should ultimately be the same throughout the furnace so that no one area of the furnace will wear out before the others, and when the furnace is shut down, all areas will require replacement of refractories. As one witness explained the goal of zoning, it is a method that means "you don't have six inches of lining in one place down to nothing in the other." (Tr. 886–87) [8]

Arranged from the lowest to the highest quality basic bricks in terms of wear are chemically bonded (used in open hearth, electric arc and argon oxygen decarburization furnaces), regular burned (open hearth, AOD, electric arc), direct bonded (open hearth, electric arc, AOD), tar bonded (basic oxygen) and tar impregnated (basic oxygen).

With the exception of tar bonded and tar impregnated refractories, the open hearth, electric arc and AOD furnaces can generally utilize any of the other basic refractories. The basic oxygen furnace uses almost exclusively tar bonded or tar impregnated refractories and these refractories have virtually no application outside the basic oxygen furnace.

[3] *Brown Shoe Co.* v. *United States,* 370 U.S. 294 (1962).
[4] *United States* v. *Continental Can Co.,* 378 U.S. 441, 449 (1964).
[5] This furnace, referred to as AOD, is used to further refine steel produced in the electric arc furnace. (Tr. 1313)

The placement of bricks in a furnace appears to be as much an art as it is a science. Furnaces of identical design will utilize different bricks in the same zone and even the type of refractory used in a given zone of a given furnace will change from shutdown to shutdown. Among the factors that affect wear, and hence affect the type of refractory to be used, are the formula used to make the various qualities of steel (Tr. 1281), steelmaking practices (Tr. 125–26), size of the ingot to be manufactured (Tr. 1189), the source of scrap steel (Tr. 1121) and the level of steel production. (Tr. 1877)

Performance characteristics of refractories are affected by the raw material comprising the brick or specialty. Specifically, the quality, the ratio (*e.g.,* magnesite to chrome) and the type of raw material all affect performance. Still, refractories comprised of different raw material may be substitutes for each other. As an example, A.P. Green recommends the use of magnesia brick in the subhearth of an electric arc furnace, but the firm also recognizes that a cheaper chrome/magnesite brick would be suitable. (CX 245F)

As to the substitution of specialties for bricks and the reverse, specialties, like bricks, are comprised of chrome, magnesia or dolomite, and are used by the steel industry in the open hearth, electric arc and basic oxygen steelmaking furnaces. The Kaiser refractory handbook (CX 95Z–91) describes specialties "as companion products used in connection with—and sometimes instead of—basic brick." Specialties may be used as "initial lining materials and as maintenance materials to maximize furnace lining life" to reduce the frequency with which the furnaces must be relined. (CX 95Z–91) In lining each type of steelmaking [9] furnace, bricks and specialties are directly substituted for one another: Tr. 576 (open hearth furnaces); Tr. 577, 760 (basic oxygen furnaces), and Tr. 396, CX 254"O" (electric arc furnaces). Among furnaces, then, the ratio of brick to specialties will vary. To illustrate, in a basic oxygen furnace from 2–1/2 lbs. to 5 lbs. of brick will be used per ingot ton of steel produced. As the poundage of bricks increases, there is a proportionate decrease in the amount of specialties, and *vice versa.* (Tr. 417)

Because there are numerous differing performance demands upon basic refractories and because almost every refractory type will meet some particular demand better than any other refractory, there is not *perfect* interchangeability and in some limited cases none at all among basic refractories. However, where substitution is not recommended or possible, other factors, such as production flexibility, may link the products.

The strongest argument against including all basic refractories in an overall basic refractory product market based on interchangeability of use is the fact that tar impregnated and tar bonded refractories are used exclusively in the basic oxygen furnace and are not employed to any significant extent in any other steelmaking process. If interchangeability of use were the sole criterion for determining the relevant line of commerce we would exclude these refractories. But as we discuss in detail below, the record shows sufficient production flexibility between the producers of the so-called BOF refractories and other basic refractories to persuade us that these tar-strengthened bricks belong in the overall basic refractory market. [10]

Respondent also contends that non-basic refractories are frequently substituted for basic refractories so that an overall market should not exclude, at least if the market is to be based on end use criteria, the non-basic refractories. Quite clearly in some zones in steelmaking, glassmaking, and other industries that utilize basic refractories non-basic refractories may be, and are, employed. The ALJ's response to this, with which we agree, was that non-basic/basic substitution occurs only in extremely limited "grey areas," comprising merely 2%, for example, of the electric arc furnace. And even in such limited areas, some steelmakers will use non-basic refractories while others will use basic refractories without thought of substitution. Thus, even in these so-called grey areas there is not ready substitution of basic for non-basic or the reverse. Most importantly, even such substitution or capacity to substitute as does exist does not seriously weaken the insulation that a basic refractory producer enjoys from non-basic refractory competition. For most purposes, steelmakers, glass producers and other users of basic refractories simply cannot look to producers of non-basic refractories for price, quality or delivery options if the basic refractory market fails in any of these respects. For that reason it does not make economic sense to include non-basic refractories in the overall refractory market or in any submarket when considering the competitive impact of the subject acquisition.

Production Flexibility

Just as the bonding process and the raw material composition of refractories distinguish one refractory from another, these two factors determine the degree of flexibility in the production of refractories. Generally *all* refractories, including basic and non-basic, bricks and specialties, are subject to crushing, grinding, and in the case of bricks, pressing. The equipment is adaptable to all types and forms of refractories.[6] Thus the production process through the pressing stage remains the same no matter what raw materials are used or bonding process applied. As noted, after pressing, bricks are strengthened by a variety of bonding processes: chemical bonding, regular fired, direct bonding, tar bonding and tar impregnated. For chemical bonding, bricks are diverted to a chemical drier. (Tr. 864) When regular fired or direct bonded, bricks are sent to a [11] tunnel kiln. The kiln's temperature determines whether the refractory is regular fired (between 2750–2900° F) or direct bonded (generally above 3100° F). The changeover from regular to direct bonding takes from 12 to 24 hours while the reverse, from regular bonding to regular fired, requires 5 to 8 hours. No changeover time is required in switching to a chemical bonding process. Instead the bricks, as noted, are diverted to a chemical drier.[7]

Tar bonded and tar impregnated bricks can also be produced on the production lines utilized to produce chemically bonded, regular fired and direct bonded bricks. A tar impregnated brick is crushed, ground and pressed on the same equipment as are other refractories. After pressing, the product is burned in a tunnel kiln at approximately 2800° F and then impregnated with tar in an autoclave. The firing gives the brick a chemical bond, after which the pores of the brick are filled with tar to rid the brick of porosity. (Tr. 869) The tar bonded brick is a less strong, ceramic bonded brick that is simply mixed with the tar, pressed and "ship[ped] as it is." (Tr. 869)

Considerations other than equipment (*e.g.*, tunnel kilns, chemical bonding driers) determine the capacity of a manufacturer to change the composition of the raw material. Because it is extremely important that a refractory not contain foreign raw materials, a changeover to a different raw material presents the problem of contamination. Thus, to effect the changeover, production facilities are thoroughly cleansed of any foreign raw material, a time-consuming process of apparently varying lengths. Some witnesses testified that the process required several months, others 8 hours. (Tr. 1659) [12]

A further indicium of a market based on production flexibility is that major firms in the industry produce both products. It is, therefore, significant that firms accounting for 97% of basic brick production also produce specialties, that these firms' specialty

[6] However, only 30 to 40% of the production facility used to produce non-basic refractories could be salvaged in a changeover to basic brick production. (Tr. 670)

[7] The general manager of the U.S. Refractories Division of General Refractories testified that his firm's production line is capable of switching back and forth from the production of chemical bonded, regular fired and direct bonded basic refractories and will do so as many as twenty times over the period of a year. (Tr. 664–68)

production comprises 60% of the specialty market and that six of the ten leading basic specialty producers also manufacture basic bricks. (I.D. p. 22) It is not necessary that the record reveal (and it does not) the full extent to which these firms utilize the same production lines in the manufacture of both bricks and specialties. What is important is that a firm producing either basic bricks or basic specialties necessarily achieves the technological capacity to produce the other product. That a firm utilizes the same facilities[8] demonstrates that this is the case as does, of course, the fact that such a large percentage of firms produce both basic specialties and basic bricks.

Also relevant when considering production flexibility as a guide to determining the relevant line of commerce is evidence of common customers; of common technology in the application (in contrast to the production) of the products particularly where, as here, the industry is technology-intensive, and of common raw materials in producing both products. The record is clear in this regard—both basic specialty and basic brick producers sell to the steel industry; both must develop products that will withstand the emissions of steelmaking furnaces, and both utilize the raw materials magnesite, chrome ore or dolomite. Excerpts from the A.P. Green publication (*supra* at 4) amply demonstrate this.

Respondent argues that contamination between basic and non-basic refractories is no greater than the contamination from one *basic* raw material to another *basic* raw material so that from the standpoint of production flexibility the market is under-inclusive in excluding non-basic refractories. Respondent simplifies the record on this point; the record shows that producers that readily change from the production of basic refractories comprising different raw materials will not, because of contamination problems, introduce non-basic material on the same production line. Additionally, all firms in the market, except for the Dolomite Brick Corp. of America, utilize magnesia and chrome ore in producing basic refractories, either individually or in combination. Different performance characteristics can be imparted to a refractory by altering the ratio of these [13] two raw materials (Tr. 127) or upon changing their quality or grade.[9] When performance characteristics are affected by changing the ratio of one basic raw material to another or altering their grade and quality, no contamination problems exist and production flexibility is not inhibited at all, at least not on the basis of contamination considerations.

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[8] American Refractories Company produces a variety of basic bricks and specialties in the same facility and changes from the production of one to the other "to fit and satisfy the shipment our customer demands." (Tr. 111)

[9] *Supra* at 8.

We are thus persuaded that the level of production flexibility and interchangeability of use is sufficiently high and unique among basic refractory products that they constitute a relevant line of commerce. While in *Coca-Cola Bottling Co. of New York,* Dkt. 8992 (Jan. 23, 1979) [93 F.T.C. ———], the market was comprised of a variety of products "arrayed along a set of continua" of price and sweetness, here there is a continuum of performance characteristics. At its extremes (*i.e.,* chemically bonded and tar impregnated bricks) products share performance characteristics (and consequently, end-use interchangeability) only to a limited degree, but even those products at the extremes of the continuum are sufficiently close in production flexibility to warrant inclusion in an overall market comprised of all basic refractory products.

Submarkets

The aforementioned array of refractory products, not surprisingly, yields a number of submarkets. The complaint alleged, and the ALJ found, four: basic bricks, basic specialties, BOF (basic oxygen furnace) bricks, and conventionally bonded bricks. Basic bricks and basic specialties are a breakdown of the overall basic refractory market. BOF and conventionally bonded bricks are essentially a division of the basic brick submarket. We agree with the ALJ that these delineations make economic sense. We note, however, that the degree of distinctiveness that characterizes each [14] of these submarkets varies. This, however, does not lessen their appropriateness as relevant lines of commerce for testing the anticompetitive effect of the acquisition.

Basic Bricks and Basic Specialties

While basic bricks and basic specialties can be substituted for each other, they are often used to complement one another as well. *United States* v. *Grinnell Corp.,* 384 U.S. 563 (1966) For some purposes, only basic specialities can be utilized. As an example, for prolonging the life cycle of a refractory lining, basic specialties are rammed, cast, gunned, or troweled over or between basic bricks. (CX 91-97) Basic bricks have no similar function.[10] In addition, basic specialty

[10] The U.S. Steel's Manager of Processed Metallurgy graphically described how specialties complement the use of bricks:

> A gunning mix is a basic specialty that is applied with a pneumatic gun. It is a maintenance material. The gunning technique is used to place refractories wherein you don't have a mason . . . laying brick. You can use it to spray an area that is being worn faster than you would like. You can patch deep holes and gouges and things with a gunning mix. It is a non-contact method of applying. You can stand here and gun over about at that able. In fact, you can gun a roof of an open hearth some 20 feet away along a stick or along a pipe. (Tr. 1305)

manufacturers often do not make basic bricks and while basic brick manufacturers have the capacity to produce basic specialties, and almost invaribly do so, more often they will manufacture them in separate facilities.[11] These factors make it proper to separate basic refractory bricks and basic refractory specialties into submarkets.[12] [15]

Respondent argues that the basic brick market is overinclusive as there is insufficient interchangeability of use among all basic bricks. "BOF's do not use the same type of bricks used in OHF's" and "substantial additional equipment is needed for [producing] each [type of brick], and the flexibility of the great majority of existing plants is limited to only some of the listed types [of refractory bricks]." (RAB 25) As was pointed out in discussing the overall refractory market, incomplete interchangeability of use or incomplete product flexibility does not diminish the significance of a market or submarkets so long as one of these criteria link the products.

Respondent contends that the specialty market is also overinclusive, containing, as an example, Kaiser's P-165 (comprised of magnesite) and Lavino's Plastic-KN (made of chrome ore) which are not interchangeable. While used in the same furnaces, they are placed in different zones. This argument fails as the record shows that at the time of the acquisition both firms possessed the technological capabilities to produce the product of the other and were familiar with industry needs which both had met with an array of products. This is not a case where restrictive patents or raw material shortages or capital insufficiencies prevented either firm from developing products complementing those it was producing. A gap then in the product line of either Kaiser or Lavino in 1973 is not of great significance.[13] [16]

Conventionally Bonded Bricks

Although this market is comprised of bricks made of three different raw materials (dolomite, magnesite and chrome ore) or a combination of magnesite and chrome ore, and of three different strengthening processess: chemical bonding, regular bond and direct

[11] Forty percent of the leading basic speciality producers do not manufacture basic bricks but 97% of the basic brick manufacturers produce basic specialties. *Supra* at 12.

[12] In reaching this conclusion, we do not rely upon the ALJ's conclusion that "[p]rices for basic bricks are set without regard to the price of specialties . . . ." (I.D. p 54) as the record evidence (*i.e.*, CX 56Q) is simply too equivocal regarding the sensitivity to price changes between basic specialties and bricks.

[13] Non-basic refractory specialties and non-basic refractory bricks are properly excluded for the reasons set out in our discussion of why non-basic refractories should be excluded from the overall basic refractory market. *Supra* at 10.

bonded, there is a marked degree of flexibility in the production of all except for dolomite.[14] As we have detailed above, a manufacturer of a regular bonded refractory (which is strengthened by submission to heat in a tunnel kiln) can produce a direct bonded refractory by increasing the temperature in the same tunnel kiln.[15] The same firm can produce chemically bonded brick by diverting its production to equipment that adds chemicals to the refractory to give it strength.[16] Not only does production flexibility of this sort warrant the inclusion of chemically bonded, regular bonded, and direct bonded bricks in the same market, so does the high level of interchangeability of use of these bricks. Each of the products can be and is used in the lining of open hearth and electric arc furnaces.

Respondent is correct in pointing out that not each of the types of refractories comprising this submarket can be substituted for every other. Again, however, absolute interchangeability of use is not necessary in determining whether diverse products should be considered as an economic unit. Another argument, that there are a few zones in furnaces, such as the door in the electric arc furnace, that have special needs and utilize products outside this [17] submarket, is not persuasive. Steel manufacturers when constructing most zones in their open hearth and electric arc furnaces can only look to the producers of conventionally bonded bricks. If faced by an oligopoly of conventionally bonded brick producers, it will be of no comfort to the steel manufacturers planning to line an entire furnace that in lining the door of their electric arc furnace they may shop elsewhere.

BOF Bricks

The basic oxygen furnace brick submarket is comprised solely of tar impregnated and tar bonded bricks. These refractories are applied almost exclusively to the basic oxygen furnace and the BOF's needs are met virtually entirely by these two products.

Respondent argues that "not all BOF's or portions of BOF's are built with either tar bonded or tar impregnated bricks, and not all tar bonded and tar impregnated bricks are used in BOF's." (RAB 27) This slight departure from perfect symmetry is, however, insignificant and does not at all impair the usefulness of the basic oxygen refractory submarket as one in which to test the impact of the

[14] Conventionally bonded dolomite brick is only made by one company and does not account for a large segment of the market. Nonetheless, it should be included in the market because the degree of interchangeability of use is significant between the dolomite brick and the other conventionally bonded bricks.

[15] *Supra* 10–11.

[16] The front end of the production line (*i.e.*, through the pressing stage) is the same in producing each type of conventionally bonded brick.

subject acquisition. Respondent further argues that the market should include the fused cast brick as it has some application in basic oxygen furnaces. This brick is made by fusing refractory raw materials together into a liquid and pouring the molten material into a mold. After cooling, brick shapes are carved from the cooled mass. There is, therefore, no production flexibility of significance between fused cast brick and the basic oxygen refractory brick. The president of Harbison-Walker Refractories testified that the "bulk of the material being used in the BOF furnace . . . is 100 percent magnesia tar bonded or tar impregnated bricks." (Tr. 941) Thus, the presence of the fused cast brick as an alternative to the tar bonded and tar impregnated brick is limited and does not affect the integrity of the basic oxygen brick submarket.[17] [18]

D. Probable Effects of the Merger

The administrative law judge relied principally, though not exclusively, on statistical data in holding that the challenged acquisition "may . . . substantially lessen competition" in the five relevant product markets. Respondent does not contend that the data is unreliable from a statistical standpoint but that it is not reliable as a basis for predicting the competitive impact of the acquisition. We discuss respondent's contentions in this regard after reviewing the evidence bearing on competitive injury.

It is helpful to set out market shares and concentration figures in each of the relevant lines of commerce as found by the ALJ of the top two, four and eight firms and the market shares of Kaiser and Lavino, together with their rankings in the market, both pre-acquisition and post-acquisition.

Basic Refractories Market

	1973 Pre-Acquisition	*1973 Post-Acquisition*
Two Firm	33.18	42.48
Four Firm	53.06	62.16
Eight Firm	83.80	88.51
Kaiser (rank)	11.87 (2)	21.18 (2)
Lavino (rank)	9.30 (4)	—

[17] Respondent's contentions relating to the lack of actual competition between Lavino and Kaiser were generally raised in its analysis of relevant product markets. But since these contentions bear more on the significance of market shares, we will consider them *infra* at 21 in examining the probable effects of the merger, and in this connection market shares and concentration figures relied upon by the ALJ.

Basic Specialties Market

	1973 Pre-Acquisition	*1973 Post-Aquisition*
Two Firm	37.49	39.50
Four Firm	67.01	70.14
Eight Firm	88.30	91.43
Kaiser (rank)	14.82 (3)	17.95 (2)
Lavino (rank)	3.13 (9)	—

Basic Refractory Bricks Market

	1973 Pre-Acquisition	*1973 Post-Aquisition*
Two Firm	41.35	50.92
Four Firm	64.68	75.18
Eight Firm	94.29	96.68
Kaiser (rank)	10.49 (6)	22.70 (2)
Lavino (rank)	12.20 (3)	—

[19] *BOF Basic Bricks Market*

	1973 Pre-Acquisition	*1973 Post-Acquisition*
Two Firm	(unavailable)	(unavailable)
Four Firm	81.46	85.44
Eight Firm	98.35	99.97
Kaiser (rank)	3.97 (6)	12.07 (4)
Lavino (rank)	8.09 (4)	—

Conventionally Bonded Basic Bricks Market

	1973 Pre-Acquisition	*1973 Post-Acquisition*
Two Firm	46.44	60.48
Four Firm	75.57	84.84
Eight Firm	96.87	99.57
Kaiser (rank)	14.04 (4)	29.22 (2)
Lavino (rank)	15.17 (2)	—

Evidence other than market shares and concentration figures bearing upon the probable effect of the acquisition was also relied upon by the ALJ. The record shows that there is no reasonabl expectation that deconcentration can be anticipated through nev entrants. Exit, not entry, has marked the industry for many year Of the 159 firms producing refractories in 1956, 96 remained in 197 (RX 10B; RX 27C) Additionally, entry barriers are high (no firm h entered since 1964) so that administered pricing or other no competitive performance by the industry, while perhaps making t market inviting from an investment standpoint, will not likely be relieved by new entrants.[18]

Kaiser's "strategic plan outline" identifies three obstacles to entry:

(1) ". . . there is customer industry bias to conservatism and reluctance to endanger huge facilities on untried product. This can be a barrier to entry of new refractory companies." (CX 12Q) [20]

(2) Because "there is a continuing customer desire to extend average life, usually by upgrading the refractory used in 'critical zone' (which sets maximum life of lining)", technological and development capabilities are essential to growth and, of course, entry. (CX 12"O")

(3) Because "there are . . . situations where the supplier loses position [with buyers] if he lacks a broad line of products" (CX 12"O"), entry with a limited range of product is difficult.

The record reveals then several indicators bearing on the probable competitive impact of the acquisition: post-acquisition concentration is high, ranging (on a 4-firm basis) from 62.16% to 85.44%; the market shares of the acquired and acquiring firm are significant (Lavino's market shares, pre-acquisition, ranged from 3.3% to 15.17%, and Kaiser's, post-acquisition, ranged from 12.07% to 29.22%); concentration increased significantly among the top four firms, from 3.13% to 10.5%; entry barriers are formidable, and smaller firms have been exiting from the industry, thereby exacerbating the consequences of the loss via merger of independent competitors.

The ALJ found, and respondent agrees, that these indicators make out a *prima facie* case of Section 7 Clayton Act violation. Respondent contests, however, the significance of Lavino's market shares, arguing that the figures are not reliable predictors of the probable competitive consequences of the acquisition because Kaiser and Lavino were generally not (a) actual competitors in the relevant product markets and (b) Lavino's financial prospects were so dismal at the time of the acquisition that the company was, as was the acquired firm in the *General Dynamics* case,[19] a "far less significant factor" in the market than its market shares would otherwise indicate. We turn next to respondent's contentions relating to the lack of actual competition and then to Lavino's financial condition.

I

[18] Even if the evidence were to the contrary, little significance will be given to the lack of entry barriers in a ...tal acquisition, as the loss of a firm through acquisition is immediate and the effects through entry are "at ...ong term affair." *Ekco Products Co.*, 65 F.T.C. 1163, 1208 (1964), *aff'd*, 347 F.2d 745 (7th Cir. 1965)

[19] *United States* v. *General Dynamics Corp.*, 415 U.S. 486, 503 (1974).

Actual Competition

What we are looking for in determining whether the statistical data should be adjusted or discounted in any fashion is evidence that diverse products in the same market are not made both by the acquired and acquiring firms or by one of them. If that is the case, some adjustment of concentration figures or market position in the market may be necessary, depending upon the factors that have led the firms or firm not to produce the product, and whether it is likely that these obstacles will persist or would be readily surmountable under the appropriate circumstances. Having combed the record and respondent's briefs, we have discerned the following:

BOF Bricks

Respondent's contentions relating to this market can be reduced to two points: (1) that fused cast brick is also used in basic oxygen furnaces and so, along with tar bonded and tar impregnated bricks should be included in the BOF market and (2) that Kaiser's tar impregnated brick is not used, presumably because of its inadequate performance characteristics, in the basic oxygen furnace.

Fused cast bricks, as we have noted, are made by an entirely different process than are the tar impregnated and tar bonded bricks and so including them in a market based on product flexibility would not be warranted. However, because fused cast brick has been, as respondent asserts, utilized in basic oxygen furnaces, the universe used to determine concentration figures in this market may be understated to a small degree. (Tr. 941) Considering, however, that the four-firm concentration in the production of BOF bricks was 85.44% post-acquisition, the slight reduction warranted by the occasional use of fused cast bricks hardly suffices to render this market conpetitive. (Tr. 397)[20]

Kaiser's failure to do well in the basic oxygen furnace submarket does not affect the significance of Lavino's position. But even as to Kaiser's market position, no adjustment is necessary as nothing in the record shows that Kaiser, with its vast resources, its technological capabilities, and its experience in producing and selling refractories, would not soon develop a suitable basic oxygen brick for use in this submarket. It remained, in short, a competitive factor whose position should not in any fashion be discounted. [22]

[20] The overall basic refractory and basic brick market would similarly be affected, but to even a lesser degree as BOF bricks comprise a small portion of these markets.

Basic Bricks

While respondent does not contest the finding that the geographical market is the nation, Kaiser contends that only 25% of its basic brick production was sold to eastern steel producers and 90% of Lavino's production of basic bricks went to eastern steelmakers. This, of course, does not bear on Lavino's market position or upon concentration figures. Additionally, it is not necessary that the acquired and acquiring firms' sales be to the same customers in order for concentration figures to have significance. *RSR Corporation,* 88 F.T.C. 800 (1976), *aff'd,* CCH 1979-1 Trade Cas. ¶62439 (9th Cir. 1979). More importantly, these figures evidence the fact that Kaiser had the capacity to sell and did sell on a significant scale in the same region as Lavino, so that no adjustment is warranted.

Basic Specialties

Kaiser's magnesia ramming and gunning mix, respondent contends, is not interchangeable with Lavino's plastic chrome ore. Further, Kaiser's sales of chrome ore specialties was less than $1,000 in 1973, while Lavino sold "a small amount of magnesia ramming mix" in that year (RAB 24). The small amount of overlap between the two firms as to these specific specialties does not warrant an adjustment in market shares. Both firms clearly have the capacity to produce the products in question. That, as of 1973, great success had eluded each as to its competitor's specific product proves very little about their long term prospects, and it is these prospects that are central to determining the likely effect of the acquisition.

Conventionally Bonded Brick

Respondent claims that Kaiser's direct bonded brick, unlike Lavino's, failed to meet the performance requirements necessary for use in electric arc sidewalls and open hearth roofs and so was used in less sensitive areas in these furnaces (RAB p. 30, n. 39). The inadequacy of the Kaiser product, of course, does not diminish the significance of Lavino's market shares. At most it could indicate that Kaiser's position in the market is somewhat overstated, but only prior to the acquisition. However, this is speculative. In any event, for purposes of determining the likely competitive effect of the acquisition, the important statistical figures are those showing concentration before and after the acquisition and the market position of the acquiring firm post-acquisition. These figures are not affected by Kaiser's apparent failure in 1973 to develop a high performance chemical bonded brick. [23]

Financial Condition of Lavino

The financial condition of the acquired company at the time of the acquisition may be relevant to show (a) that a firm is faced with a "grave possibility of business failure"[21] and that the prospects of recovery through reorganization are "dim or nonexistent"[22] or (b) that the acquired firm's assets, because of circumstances beyond its control, will not strengthen the acquired firm and any increase in concentration will not persist over time. The first of these showings relates, of course, to the failing company defense and requires the additional showing that no other purchaser was available to make the acquisition.[23] Essentially, this defense is based on the notion that although an acquisition may be anticompetitive, it is in the public interest to permit the acquisition (*i.e.,* jobs that might otherwise be lost in the short run may be saved and assets that might be temporarily dissipated will continue to contribute to the economy). Respondent does not contend that the failing company defense is applicable in this case.

Respondent argues instead that the acquisition was not anticompetitive because Lavino would not have continued as a viable competitor in the sale of refractories. Respondent relies on what has come to be called the *General Dynamics* defense, but we believe that it misapplies the holding of that case. In essence, the *General Dynamics* decision stands for the commonsense proposition that an increase in concentration will not persist no matter how impressive the market shares of the merging firms at the time of the acquisition if, at the time of the acquisition, the key competitive assets of either merging party were so depleted that they could not be revivified by either the acquired *or* the acquiring firm. The Court found in *General Dynamics* that in the coal industry "a company's power effectively to compete with other companies lies in the state of a company's uncommitted reserves of recoverable coal".[24] [24]

Because United Electric Coal Companies, the acquired concern, had neither reserves nor prospects of obtaining reserves, the company was not a significant competitive factor and, more to the point, did not provide General Dynamics with the wherewithal to enhance its competitive position (as measured by its market share). Hence, neither General Dynamics' long term competitive position nor long term market concentration generally was affected as a consequence of the acquisition. The Court thus concluded that the

[21] *Citizens Publishing Co.* v. *United States,* 394 U.S. 131, 137 (1969).
[22] *Id.* at 138.
[23] *Id.* at 137.
[24] *Supra* at 502.

acquisition was not likely to be anticompetitive, even though the combined market shares of the merging companies at the time of the merger were high.

The Court did not denigrate concentration and market share figures as the best available measurement of the effects of a merger—it merely insisted that contemporaneous figures give way where it could be shown by way of an affirmative defense that they were unlikely to persist over time. Indeed, the Court indicated that market shares and probable future competitive effects could best be measured by examining uncommitted coal reserves, in effect substituting a more reliable statistical test for the traditional standard based on current production or sales. It seems clear that the Court did not intend to attach significance to every negative factor concerning a firm's operations, particularly where the evidence relates to conditions within the control of one of the parties to the merger. As the Court observed in *General Dynamics,* the evidence there "implied that United Electric *was not merely disinclined* but unable to compete effectively for future contracts." *Id.* at 506 (emphasis added).

To utilize the defense, then, a respondent must show (a) that one merging firm's market share (in this case, Lavino's) could not be imparted to the other merging firm, so that any increase in concentration will not likely persist over time, (b) that the merging firms had no control over the circumstances that weakened the position of the merging firm whose market shares will be discounted and (c) that neither firm could remedy the position of the weakened firm. Lavino's situation, assuming the worst possible case, does not meet these criteria.[25] [25]

Respondent characterizes Lavino's position as follows: "By late 1970 [irresistible market forces] had led IMC to a sound business decision to channel its capital to more productive areas and salvage what it could of its investment in Lavino. In the two ensuing years, 1971-73, new investment in the division was cut to a minimum; R&D expenditures were severely curtailed; and cutbacks were made in the sales and technical service departments. The planned expansion of the product line was cancelled; plant maintenance was deferred wherever possible; and the Newark and Freeport plants were closed and liquidated."[26]

[25] The decision in *United States* v. *International Harvester Co.*, 564 F.2d 769 (7th Cir. 1977), an opinion strongly relied upon by Kaiser, does not call for a different result here. The court there concluded that Harvester's acquisition of a 39% stock interest in Steiger Tractor, Inc., helped preserve Steiger as an independent competitor in the market rather than eliminating competition between the two firms. The court also noted that concentration had decreased slightly since the merger and several new firms were entering or about to enter the market. *Id.* at 778. Surely *International Harvester* is a most unusual case and not applicable to this matter.

[26] RAB 32.

Additional problems hampering the Lavino operation included need for capital improvements of its two production plants, substantial infusion of money to update its research and development and the expansion of its product line.

None of these problems were such that they could not be remedied with the financial resources, technical know-how, and general experience of Kaiser or other similarly situated concerns, including IMC. Thus, while "Lavino was unable to make high quality magnesia products at the Gary plant [because of IMC's decision not to improve that facility],[27] with Kaiser capital the plant was modified to do so." (RAB 41 n. 56) And further, "Kasier . . . improved the performance of the Lavino plants and has used them in the improvement of its own products . . . ." (RAB 42)

Kaiser's position was enhanced not only because of the addition of Lavino plants. Lavino's valuable long term, low cost supply contract guaranteed respondent a source of magnesite. (RX 364; Tr. 2414) Additionally, the sophisticated research and development capability that had characterized Lavino's operations was folded into and came to dominate Kaiser's R&D in basic refractories. For four years following the acquisition, four of the five professionals comprising Kaiser's R&D were former Lavino personnel. (Tr. 2717–18; 2723–26) [26]

Not surprisingly, then, in 1974 the North America Refractories Co., a competitor of Kaiser, in reviewing the strengths of firms in the industry, had this to say about the prospects of Kaiser-Lavino: "The Kaiser-Lavino merger will make for a stronger competitor because of their [presumably both Kaiser's and Lavino's] production capacity and research capability." (RX 400D) In 1976 the same competitor noted that Kaiser had "generated impressive record performances resulting in penetration into our markets." (RX 408F)

This, then, is a case where the acquiring firm, Kaiser, gained viable and valuable assets which enabled it to aggrandize its already formidable market positions in several highly-concentrated markets and submarkets.[28] As well as increasing the size of the acquiring firm, the merger has wrought substantial increases in concentration in the relevant markets, and there is no reason suggested by the

[27] Counsel for respondent conceded at oral argument that either IMC or another company could have achieved what Kaiser had with Lavino but IMC had not because "they wanted out". (Transcript of Oral Argument 4073,74)

[28] Respondent contends that the acquisition was procompetitive as Kaiser is a more vigorous and effective competitor as a consequence of the acquisition. The strengthening of a competitor cannot be equated with strengthening competition. Certainly this is clear when, as here, enhancing the acquiring firm's position means the loss of an independent decisionmaker and an increase of concentration. By contrast, as we have noted, in *International Harvester* competition was enhanced by the "acquisition" because the acquired firm remained independent and gained competitive vigor it would have lost except for Harvester's infusion of capital *and* because concentration decreased.

record to believe that these high market shares among the top firms will not persist. It was precisely to prevent such increases in concentration, with the concomitant opportunities for interdependent oligopolistic behavior they bring with them, that Section 7 was enacted, and the merger of Kaiser and Lavino clearly falls within its proscription. [27]

E. Relief

To restore competition in markets adversely affected by an illegal acquisition, divestiture is commonly considered the most "appropriate relief."[29] When, as here, the acquiring and acquired firms were competitors in the same markets, divestiture will "minimally bring about deconcentration in the adversely affected markets and may additionally serve to restore competition in the relevant markets by lowering or checking the rise of entry barriers, decreasing the possibility of entrenchment and re-establishing toehold firms."[30]

The purpose of an effective order, then, must be to divest Kaiser of the assets it obtained by the illegal acquisition and to restore Lavino as a viable entity of roughly the same competitive capacities it possessed before the acquisition. Because Kaiser was not required to and did not hold separate the Lavino assets it had acquired in 1973, and further because in order to survive and thrive in the relevant markets the new Lavino must possess assets other than plants, customer lists and the like, an effective order must necessarily require more than a simple, straightforward divestiture of what Kaiser acquired in 1973.

Mindful of these considerations, the ALJ required (1) the divestiture of all assets of Lavino acquired by Kaiser (Order provision I); (2) that Kaiser not hire any employee of Lavino for three years (IV); (3) that know-how, patents and trade secrets developed since the acquisition and for a period of five years after the divestiture be made available to Lavino without charge (IX); (4) that the raw material magnesia obtained from Harbison-Walker be made available either by assignment from that company or through Kaiser for three years following the divestiture (X); (5) that Kaiser assist in hiring and establishing a research and development staff for the new Lavino (XI); (6) that Kaiser provide Lavino a list of customers who purchased basic refractories from Kaiser within the three year period of the divestiture (XII); and (7) that Kaiser not solicit for two years customers that purchased from Lavino during the year prior to

[29] *United States* v. *E. I. duPont de Nemours & Co.*, 366 U.S. 316, 328 (1961).

[30] *Litton Industries, Inc.*, 85 F.T.C. 382 (1975).

the acquisition if they did not deal during that year with Kaiser (XVIII). [28]

Because the new Lavino's success will depend in large part upon its R&D capabilities, it is appropriate that the order provide for technical assistance to the new Lavino. As drafted by the ALJ, the order would do this by requiring Kaiser to provide know-how, patents, and trade secrets developed after the divestiture; to assist Lavino in establishing its own research and development capacity, and to divest both the patents acquired as a result of the acquisition of Lavino and the improvements on these patents.

With one modification we believe that each of these provisions is proper and necessary to the development of a viable Lavino. Respondent objects particularly to the provision that would require Kaiser to share technological know-how for a period of five years following the divestiture. We agree that once Lavino's research and development staff is in place it should not be necessary and might even be counterproductive for the new Lavino to have access to Kaiser's research and development. Sharing of research and development can have a depressing effect on both companies, inhibiting Kaiser's inventiveness and dampening the need for bold initiatives by Lavino. The order will, therefore, require that Kaiser provide research and development know-how until such time as Lavino's research and development staff has been hired. Because the professional research and development staff will need *some* nurturing, Kaiser will also be required to share research and development for six months following that date. The ALJ considered a period of one year from the divestiture long enough for Kaiser to be obligated to assist Lavino in establishing a research and development staff. We agree, and so that provision is so limited, and the period that Kaiser will be required to share the fruits of its research and development will not exceed 18 months following the divestiture.

We also agree with respondent that the antisolicitation provision should not be included in the order. This is an industry in which the relevant products differ in quality from one manufacturer to the next and so the effect of denying a customer access to even one seller's products (whether by an illegal merger or by an overzealous order provision) may have adverse competitive implications. Because of this and because the benefits that Lavino would gain from the provision are marginal, the provision is not warranted and will not be included in the order. [29]

We agree with the ALJ that the new Lavino should have access to magnesia pursuant to the Harbison-Walker supply contract, either by assignment directly from Harbison-Walker or through Kaiser. We agree with respondent that the price of the raw material if acquired from Kaiser should be the price that Kaiser pays Harbison-Walker. Accordingly, the provision drafted by the ALJ relating to the supply contract, without the modification recommended by complaint counsel, is adopted.

The provision recommended by the ALJ prohibiting the hiring by Kaiser of Lavino employees for three years is too harsh for the purpose intended — to prevent the pirating of Lavino personnel by Kaiser. Complaint counsel recommend a modification, with which we agree, that would prohibit hiring of Lavino personnel without Commission approval. In this way any unreasonable stripping of the new Lavino can easily be forestalled without unduly hampering the natural exchange of personnel among competitors.

Respondent raises questions with respect to other provisions in the order recommended by the ALJ. In Paragraph VIII the ALJ requires that Kaiser not acquire a firm producing basic refractories without Commission approval for a period of fifteen years. Respondent contends that such a moratorium should not exceed the ten years ordinarily imposed in Section 7 orders. We agree, because there is nothing in the record showing that a period longer than the customary ten years for such a provision is warranted.

Complaint counsel recommend several additions and modifications to the order recommended by the ALJ. They would add two provisions relating to the preservation of assets pending divestiture. These will be included in the order. Complaint counsel also suggests a modification of the moratorium provision which will make it clear that it applies to acquisitions of firms with a presence in the United States basic refractories market. The provision is so modified.

Respondent presses for a proviso that would require that the purchase price exceed the liquidation value of the Lavino assets. Only in this way can the Commission be assured, respondent argues, that a purchaser will not raze the Lavino plants and develop shopping centers on their sites. Respondent's argument assumes that no purchaser would develop the Lavino assets along the lines envisioned in this opinion if the purchase price is less than the liquidation value of the assets. No such assumption is warranted. We lo recognize, however, that the purchase price as it relates to the iquidation value of the company is a factor to be considered in etermining whether a purchaser is acceptable. But the problem of nding an acceptable purchaser is a matter for compliance. We will ot unduly complicate the quest by the imposition of provisos and nditions that may be deficient in failing to anticipate the dimen- ons of the task.

Concurring Opinion of Commissioner Pitofsky

I agree that the acquisition by Kaiser of the assets of the Lavino Division of IMC violates Section 7, and agree with the reasoning of the majority opinion except that portion which finds the existence of an overall relevant product market consisting of basic refractory bricks and basic refractory specialties. Nevertheless, I concur in the opinion since I agree that the four other relevant product submarkets can be sustained and the combined market shares in those markets are sufficient to support a finding of a violation.

With respect to the more inclusive brick-specialty product market, the majority opinion recognizes that there are few instances in which brick or specialty are direct substitutes. Both categories are manufactured in most plants in the refractories business, but the Administrative Law Judge found that there is no cross-elasticity between the two:

> Prices for basic bricks are set without regard to the price of basic specialties and different refractories' producers are the price leaders in each market. (Findings 131, 158; CX 56 Q.) Basic bricks are recognized as a distinct product market by the steel companies and by refractories' manufacturers. (Initial Decision, p. 54.)[1]

[2] Given that finding, there ordinarily would be little reason to expect that bricks and specialties could be in the same product market. In briefing and oral argument, counsel supporting the complaint attempted to surmount this apparent separateness of the brick and specialty markets by arguing along the lines of *Philadelphia National Bank*[2] that bricks and specialties belong in the same market on a "cluster" theory — *i.e.,* that apparently different products with different prices and uses may be in the same relevant product market if they are as a group sufficiently distinctive to be free of effective competition from other products and if customers, as a practical matter, do all or some of their shopping for some of those products from the same sellers at the same time. 374 U.S. 321, 356. L. Sullivan, *Antitrust* 59–61 (1976). While it is true that bricks and specialties are often sold "under the same roof" in many refractory plants, it does not follow that there is any economic reason why customers would choose to do their brick purchasing and specialty purchasing from the same company. [Cf. *United States* v. *Phillipsburg National Bank,* 399 U.S. 350, 359–360 (1970).] Indeed, there is a finding by the administrative law judge that basic specialties and

[1] The majority has some doubts about, but does not explicitly reject, this finding. Even if the finding were rejected, it would not affect this opinion since it would still be the case that there would be no evidence of substantial cross-elasticity of demand between bricks and specialties.

[2] *United States* v. *Philadelphia National Bank,* 374 U.S. 321 (1963).

basic bricks are purchased by different persons in the steel industry, basic specialties being sold to the steel producing superintendent and basic bricks to the masonry superintendent (Finding 130). Given that background and the absence of economic linkage, the majority, in my opinion, has wisely not written its opinion supporting a brick-specialty market on a "cluster" theory.

Instead, the key argument by the majority turns on the concept of production or supply flexibility. Thus, the majority assumes that if the price of bricks or specialties were to rise, it would not follow that purchasers would switch from one category to the other. The majority opinion predicts, however, that manufacturers would switch existing machinery producing one product category in order to satisfy demand for the higher priced product, and this ready transferability of production capacity puts the two categories in the same product market. There is an administrative law judge finding on which the majority relies to the effect that the two product categories — bricks and specialties — are manufactured on some of the same equipment and that a refractories manufacturer may switch from basic bricks to basic specialties in response to consumer demand (Finding 103). [3]

Supply substitutability, of course, can be a factor leading to a finding of a single relevant market, and can be a useful concept in tracing the dynamics of product competition. *United States* v. *Columbia Steel Co.*, 334 U.S. 495 (1948); 2 P. Areeda & D. Turner, *Antitrust Law*, §526 (1978). Here, the record clearly shows that there is a *capacity* for supply substitutability, *i.e.*, that there is some possibility at some point that machines currently committed to manufacturing bricks could be converted to manufacturing specialties and vice versa. I do not believe, however, that is adequate to support a finding that the two product categories are in the same relevant product market. First, there is no evidence of actual switching of equipment from bricks to specialties, or vice versa, in response to changing conditions of supply and demand. Also lacking is evidence to demonstrate that machinery would be shifted from one category to the other relatively promptly in response to relatively modest price changes.[3] Without a record to show actual or likely shifts of production resources, there is no reason to expect that manufacturers of bricks, in determining what price to charge, would

[3] Since a specialty is in some sense an intermediate product on the way to producing brick, it is perhaps plausible to assume that brick makers could switch production to specialties although even here there is a cost factor involved. There is absolutely no reason to speculate, and certainly no evidence, that a specialty manufacturing line could ever be switched over to brick production relatively promptly or at relatively modest cost. In similar circumstances, the Commission declined to find a "health and beauty aids" market when there was no evidence that the cosmetics manufacturers could "step up" to the more complex level of quality control and technology of the pharmaceutical manufacturers. *Sterling Drug, Inc.*, 80 F.T.C. 477, 593-94 (1972).

regard specialty competition as sufficiently direct and substantial to take into account.[4]

In the absence of a record to support a finding of supply substitutability, I would not consider that there was a brick-specialty relevant market.

FINAL ORDER

This matter having been heard by the Commission upon the appeal of respondent from the initial decision, and upon briefs and oral argument in support thereof and in opposition thereto, and the Commission for the reasons stated in the accompanying Opinion having determined to sustain the initial decision with certain modification:

It is ordered, That the initial decision of the administrative law judge be adopted as the Findings of Fact and Conclusions of Law of the Commission, except to the extent indicated in the accompanying Opinion. Other Findings of Fact and Conclusions of Law of the Commission are contained in the accompanying Opinion.

It is further ordered, That the following order to cease and desist be, and it hereby is, entered:

I

It is ordered, That

Respondent Kaiser Aluminum and Chemical Corporation (hereinafter "Kaiser"), a corporation, and its officers, directors, agents, representatives, employees, subsidiaries, affiliates, successors, and assigns, shall divest all assets, title, properties, interests, rights and privileges [2] of whatever nature, tangible and intangible, including without limitation all real property, buildings, machinery, equipment, tools, raw materials, reserves, inventory, customer lists, trade names, patents, trademarks and other property of whatever description acquired by Kaiser as a result of its acquisition of the basic refractories segment of the Lavino Division of International Minerals & Chemicals Corporation (hereinafter "Lavino" and "IMC") together with all additions and improvements to said property which have been made subsequent to the acquisition. Such divestiture shall be absolute, shall be accomplished no later than one year from the

[4] In several respects, the failure of proof situation with respect to the record here is like that in *Brown Shoe Co. v. United States,* 370 U.S. 294 (1962) where the Supreme Court rejected a government argument that there was an overall relevant product market of footwear (rather than separate mens, womens, and childrens shoes markets) because "the District Court made limited findings concerning the feasibility of interchanging equipment in the manufacture of non-rubber footwear." 370 U.S. at 325 n. 42.

effective date of this order, and shall be subject to the prior approval of the Federal Trade Commission.

II

The divestiture described in Paragraph I herein shall be accomplished absolutely to an acquiror and in a manner approved in advance by the Federal Trade Commission so as to transfer Lavino as an ongoing business and a viable, competitive, independent concern.

III

Pending divestiture, no substantial property or other asset referred to in Paragraph I herein shall be sold, leased, otherwise disposed of or incumbered, other than in the normal course of business, without the consent of the Federal Trade Commission.

IV

No individual employed by the new owner of the divested assets and engaged in research, manufacture or sale of basic refractories at any time during the period beginning on the date of the divestiture specified in Paragraph I herein and extending for three years, shall be hired by Kaiser without the consent of the Federal Trade Commission.

V

Pending any divestiture required by this order, Kaiser shall not allow the deterioration of the property specified in Paragraph I in a manner that impairs the marketability of the business. [3]

VI

Pursuant to the requirements of Paragraph I, none of the property or business acquired or added by Kaiser shall be divested to anyone who is an officer, director, employee or agent of Kaiser or is in any other way controlled or influenced by Kaiser, or to anyone who owns or controls, directly or indirectly, more than one percent of the outstanding shares of the capital stock of Kaiser or to anyone who is not approved in advance by the Federal Trade Commission.

VII

For a period of ten (10) years from the date this order becomes final, Kaiser shall cease and desist from acquiring or acquiring and holding directly or indirectly, through subsidiaries or otherwise, without the prior approval of the Federal Trade Commission, the whole or any part of the stock, share capital or assets, or any other interest in any company engaged in the business of manufacturing, distributing, or selling basic refractories in or to the United States.

VIII

Kaiser shall provide upon request of the purchaser, without charge, the use of all know-how, patents, and trade secrets developed by the Kaiser Refractories Division's basic refractories research and development staff from the time of the acquisition by Kaiser of the Lavino assets to six months after the date that Lavino has established a staff for research and development as described in Paragraph X, provided that this period shall not extend beyond the period of eighteen (18) months from the date of the divestiture specified in Paragraph I.

IX

For a period of three years from the date of the divestiture described in Paragraph I, if requested by the purchaser for its own use, Kaiser shall provide such amounts and grades of magnesia as are requested, with the maximum amounts, grades and prices to the purchaser limited to that receivable by Kaiser under the supply contract (or any renewal pursuant thereto) obtained by Kaiser from Harbison-Walker in the acquisition of the Lavino assets. Kaiser shall provide the purchaser reasonable access to documents sufficient to allow the purchaser to determine whether Kaiser is in compliance with the provisions of this paragraph. [4]

X

For a period of one year from the date of the divestiture described in Paragraph I, Kaiser shall, if requested by the purchaser, without charge, in good faith, assist the purchaser in hiring and training a staff for research and development and for sales of basic refractories. Kaiser shall, in this regard, pay the expense of obtaining, through an employment agency picked by the purchaser, competent, technically trained, basic refractories salesmen and research and development scientists, and their supervisors. The number of such personnel shall not exceed the number employed by Lavino on November 9, 1973.

XI

At the time of the divestiture required by this order, Kaiser shall make available to the purchaser of the property and business, a list of all of Kaiser's customers for basic refractories products who have purchased said products from respondent within three years prior to the divestiture.

XII

Any dispute between Kaiser and the purchaser arising under Paragraphs VIII–XI of this order shall be resolved at the option of either Kaiser or the purchaser pursuant to the Commercial Arbitration Rules and the procedures of the American Arbitration Association. If arbitration is invoked by either party, such arbitration shall be exclusive and in lieu of any other common law rights. The arbitrator shall be selected by the parties from the panel of arbitrators of the American Arbitration Association or by the Federal Trade Commission in the event that the parties are unable to agree; said arbitrator shall be empowered to determine the merits of any dispute arising under Paragraphs VIII–XI of this order, and assess the costs of arbitration; the decision of said arbitrator shall be final and binding upon the parties and judgment thereon may be entered in any court of competent jurisdiction. Arbitration shall be no cause for delay; and in the event of a default by either party in appearing before the arbitrator, pursuant to advance written notice, the arbitrator is authorized to render a decision upon the testimony of the party appearing.

XIII

One year from the effective date of this order, and [5] on the anniversary date of each year thereafter until the expiration of the prohibitions in Paragraph VII of this order, Kaiser shall submit a report in writing to the Federal Trade Commission listing all acquisitions, mergers, and agreements to acquire or merge made by Kaiser relating in any way to the production or sale of basic refractories; the date of each such acquisition, merger or agreement; the products involved and such additional information as may from time to time be required.

XIV

Within thirty days from the effective date of this order and every sixty days thereafter until it has fully complied with Paragraph I of this order, Kaiser shall submit a verified report in writing to the Federal Trade Commission setting forth in detail the manner and form in which it intends to comply, is complying or has complied therewith. All such reports shall include in addition to such other information and documentation as may hereafter be requested: (a) a specification of the steps taken by Kaiser to make public its desire to divest Lavino; (b) a list of all persons or organizations to whom notice of divestiture has been given; (c) a summary of all discussions and negotiations together with the identity and address of all interested persons or organizations, and (d) copies of all reports, internal memoranda, offers, counteroffers, communications and correspondence concerning said divestiture.

XV

Kaiser shall notify the Commission at least thirty days prior to any proposed changes by it which may affect compliance obligations arising out of this order.

IN THE MATTER OF

GENERAL MOTORS CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2966. Complaint, May 18, 1979 — Decision, May 18, 1979

This consent order, among other things, requires a Detroit, Mich. motor vehicle manufacturer to cease misrepresenting the manufacturing source of engine options and the availability of standard or optional equipment. The order also requires the firm to make designated disclosures regarding the manufacturing source, ordering code, and availability of each engine option offered for the model years 1979 through 1981; notify dealers promptly of engine option substitutions; and provide them with the replacement parts and maintenance information necessary to service such equipment. Additionally, the company would be prohibited from using any wholesale order system which could prevent dealers from designating specific options requested by purchasers.

Appearances

For the Commission: *Sharon J. Devine, William W. Jacobs* and *John M. Mendenhall.*

For the respondent: *Robert C. Weinbaum,* Detroit, Mich. and *Richard W. Pogue, Jones, Day, Reavis & Pogue,* Cleveland, Ohio.

COMPLAINT

The Federal Trade Commission, having reason to believe that respondent General Motors Corporation, a corporation, has violated the provisions of Section 5 of the Federal Trade Commission Act and that a proceeding by it in respect thereof would be in the public interest, issues this complaint:

PARAGRAPH 1. Respondent, General Motors Corporation, is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 3044 West Grand Boulevard, Detroit, Michigan.

PAR. 2. Respondent is now and has been, engaged in the manufacture, distribution, sale, promotion and advertising of various products including passenger cars.

PAR. 3. Respondent maintains, and at all times mentioned herein has maintained, a substantial course of trade in said products in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. Respondent has represented that certain standard and optional equipment is manufactured by the particular division of respondent that built the passenger car.

PAR. 5. In fact, the equipment set forth in Paragraph Four is manufactured by a division other than that represented.

Therefore, the representations set forth in Paragraph Four were, and are, an unfair and deceptive practice.

PAR. 6. Respondent has represented to purchasers that various standard and optional equipment is available in respondent's passenger cars.

PAR. 7. In fact:

(a) Some of the standard and optional equipment was not made available as represented by respondent;

(b) In some instances, respondent substituted other equipment for standard and optional equipment represented by respondent to be available; and

(c) In some instances, respondent delivered passenger cars which were ordered on behalf of a retail purchaser and which were equipped with standard or optional equipment different from that ordered by the retail purchaser.

Therefore, the representations set forth in Paragraph Six were, and are, an unfair and deceptive practice.

PAR. 8. Respondent has failed to disclose in advertising and has failed to provide notice and advertising to its dealers adequate to disclose to purchasers that for certain passenger cars:

(a) Certain standard and optional equipment offered for sale in certain lines of passenger cars is manufactured by a division other than the division under whose name such line is distributed or sold.

(b) Certain standard and optional equipment is not available in lines for which respondent has represented it as available.

(c) Other standard and optional equipment has been substituted for the unavailable equipment.

(d) Substituted standard and optional equipment differs from the unavailable equipment.

(e) An order by a retail purchaser for particular standard and optional equipment would not necessarily result in an order placed on behalf of the purchaser which specifies that particular equipment.

(f) An order placed on behalf of a purchaser for certain standard and optional equipment previously represented as available could result in delivery of a passenger car without such equipment or with different equipment.

PAR. 9. Respondent has failed to make available information and parts adequate to enable its dealers to fulfill warranty obligations to purchasers of passenger cars equipped with substituted equipment (referred to in Paragraphs Seven and Eight).

PAR. 10. Respondent has failed to make available to purchasers of respondent's passenger cars equipped with substituted equipment accurate information regarding recommended maintenance intervals and regular maintenance replacement parts.

PAR. 11. The facts set forth in Paragraphs Eight, Nine, and Ten are material to consumers. Thus, respondent has failed to disclose material facts which, if known to purchasers, would be likely to affect their consideration to purchase respondent's items. Therefore, these practices were, and are, unfair and deceptive practices.

PAR. 12. In the course and conduct of its business, and at all times mentioned herein, respondent has been, and is now, in substantial competition in or affecting commerce with corporations, firms, and individuals engaged in the sale of merchandise of the same general kind and nature as merchandise sold by respondent.

PAR. 13. The use by respondent of the aforesaid false, misleading, and deceptive statements, representations, acts and practices, directly or by implication, has had, and now has, the capacity and tendency to mislead members of the public into the erroneous and mistaken belief that said statements and representations were, and are, true and complete, and into the purchase of substantial quantities of respondent's products and services by reason of said erroneous and mistaken belief.

PAR. 14. The acts and practices of respondent, as herein alleged, were and are all to the prejudice and injury of the public and of respondent's competitors and constituted, and now constitute, unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Cleveland Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent General Motors Corporation (GM) is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 3044 West Grant Boulevard, in the City of Detroit, State of Michigan.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

I

For purposes of this order, the following definitions shall apply:

A. The term "GM" shall mean General Motors Corporation, and all of its divisions, its successors, assigns, officers, representatives, agents, and employees, acting directly or through any subsidiary or other device.

B. The term "franchised GM passenger car dealer" shall mean any person, partnership, or corporation which is a party to a franchise agreement with GM to purchase new GM passenger cars for resale to purchasers.

C. The term "manufacturing source" shall mean the GM division or entity by which the item referred to was produced.

D. The term "line" shall mean each make and model of passenger car manufactured by General Motors Corporation and distributed or sold under the Chevrolet, Pontiac, Buick, Oldsmobile or Cadillac name.

E. The term "engine option" shall mean any engine designated by a GM ordering code number (including the standard engine) offered by GM as factory-installed equipment. For purposes of this order, each engine option shall be assigned a single, unique ordering code designation for a given model year which does not vary across division lines.

F. The term "material difference" shall mean any difference which results in a significant difference in engine performance, including but not limited to any difference in Environmental Protection Agency (EPA) fuel economy ratings, mileage intervals in excess of 1,000 miles for recommended engine maintenance, horsepower and displacement, or which results in a difference of regular maintenance replacement parts.

G. The term "substituted engine" shall mean an engine option installed in any GM line in any area of the country as a replacement for an engine option offered for that line in the same model year, but which is unavailable in such line or area, if the replacement engine option

(1) is produced by a division other than that which produced the engine option to be replaced; or

(2) has any "material difference" from the engine option to be replaced.

H. The term "option" shall mean an item of equipment to be installed in a new GM passenger car for which GM provides purchasers a choice of alternatives.

I. The term "purchaser" shall mean a potential buyer, potential lessee, buyer and lessee of any new GM passenger car, but shall not include a franchised GM passenger car dealer.

II

It is hereby ordered, That GM is prohibited from misrepresenting as of the time the representation is made by GM:

A. The manufacturing source of any engine option; and

B. That an option or item of standard equipment offered for a new GM passenger car is available if in fact it is not.

III

It is further ordered, That GM is prohibited from displaying the name of any GM car division on any engine or visible attachment to the engine under the hood of a new GM passenger car, including the air filter cover, unless the engine is manufactured by that division.

IV

It is further ordered, That if:

A. GM furnishes or has furnished, during or in preparation for any model year, any information to any franchised GM passenger car dealers regarding any engine offered for any GM line for any model year, and

B. the engine described in the information provided to such dealers is to be or has been replaced by a substituted engine for that model year,

GM shall notify such dealers in writing, with respect to the affected lines handled by them, forthwith after the decision to substitute has been made. Such written notification shall include the lines in which the substituted engine is offered, its manufacturing source, ordering code number, designation used in the vehicle identification number to identify the type of engine option, and any material differences between the substituted engine and the engine to be replaced.

V

It is further ordered, That, for the 1979, 1980, and 1981 model years, GM shall furnish to all franchised GM passenger car dealers point-of-sale literature for distribution to purchasers in dealer showrooms disclosing clearly and conspicuously the engine options available in the GM lines carried by the dealer, and, for each engine option, the lines and areas of the country in which it is or is not available, its manufacturing source, and its ordering code designation. GM shall take such steps as are reasonably necessary to furnish such information to such dealers on a current basis. GM shall request, in writing, that such dealers display such materials in a conspicuous, accessible area of the dealer showroom.

VI

It is further ordered, That GM shall clearly and conspicuously disclose the following statement in all print advertising for the 1979 model year, and in the principal new car point-of-sale catalogs for the 1979, 1980, and 1981 model years, which contain any reference to the engine (including any representation regarding EPA fuel economy) in any GM line, group or lines or division, in which an engine option produced by a division different from the division under whose name the passenger car is distributed is offered:

> *(Line, group of lines, divisional products)* is (are) equipped with GM-built engines produced by various divisions. See your dealer for details.

VII

It is further ordered, That, for the 1979, 1980, and 1981 model years:

A. GM shall clearly and conspicuously disclose, on a "window sticker" attached by GM to each new passenger car, or on the price information labels required by the Automobile Information Disclosure Act (15 U.S.C. 1232), the engine ordering code, and the manufacturing source of the engine installed in that car.

B. GM shall disclose in each owner's manual, maintenance chart or other maintenance information provided to a purchaser of a new GM passenger car, the accurate information customarily furnished regarding recommended maintenance intervals and regular maintenance replacement parts applicable to the engine installed in that car.

VIII

It is further ordered, That GM shall make available, subject to *force majeure,* labor disruptions, and other causes outside GM's control, replacement parts and repair and maintenance information to franchised GM passenger car dealers adequate to allow such dealers to provide GM warranty service to purchasers of new GM passenger cars equipped with any substituted engine to the same extent as it does in the case of new GM passenger cars equipped with non-substituted engines.

IX

It is further ordered, That this order shall be limited in its application to sales of new GM passenger cars in the United States and its territories.

X

It is further ordered, That:

A. GM is prohibited from utilizing a wholesale ordering system whereby its franchised GM passenger car dealers may not designate the specific options, other than standard equipment, requested by the purchaser. GM shall notify its dealers in writing that purchasers should be given the opportunity to designate the specific options ordered. Provided, that GM shall indicate when an option is required to be paired with another specific option.

B. For the 1979, 1980, 1981, 1982, and 1983 model years, GM shall advise its franchised GM passenger car dealers in writing whenever

GM plans to build or has built a passenger car with options other than as ordered by the dealer. GM will disclose on such writing the following language:

> Notify customer promptly of any changes indicated. If unacceptable, contact zone for disposition.

C. For the 1979, 1980, 1981, 1982, and 1983 model years, GM shall clearly and conspicuously disclose in all principal new car point-of-sale catalogs the following statement:

> Some options may be unavailable when your car is built. Your dealer receives advice regarding current availability of options. You may ask the dealer for this information. GM also requests the dealer to advise you if an option you ordered is unavailable. We suggest you verify that your car includes the options that you ordered or if there are changes that they are acceptable to you.

XI

It is further ordered, That:

A. GM shall notify the Commission at least thirty (30) days prior to any proposed change in the corporation such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of this order.

B. GM shall, within sixty (60) days after the effective date of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

IN THE MATTER OF

INLAND EMPIRE ROOFING CONTRACTORS ASSOCIATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2968. Complaint, May 22, 1979 — Decision, May 22, 1979

This consent order, among other things, requires a Spokane, Wash. roofing association to cease entering into agreements with others to establish and maintain terms of guarantees, prices, or other conditions of sale in connection with the sale of roofs and related services; suggesting that members adhere to any particular price, guarantee, or other condition of sale; and limiting by any means a member's right to give any guarantee, price or other term or condition of sale to its customers. The association is also prohibited from investigating and/or policing its members with regard to prices charged and guarantees imposed in the sale of their products and services.

Appearances

For the Commission: *Stevan D. Phillips.*

For the respondent: *Harold J. Triesch,* Spokane, Washington.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Inland Empire Roofing Contractors Association, an unincorporated association, hereinafter sometimes referred to as respondent, has violated the provisions of the Federal Trade Commission Act, as amended, as more particularly set forth herein, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Inland Empire Roofing Contractors Association is an unincorporated association organized, existing, and doing business under and by virtue of the laws of the State of Washington. Respondent's membership presently consists of nine (9) roofing contractors located in eastern Washington and western Idaho. It consisted of twelve (12) roofing contractors at the time the acts referred to herein occurred. Its office is located at East 130 Sprague Ave., Spokane, Washington.

PAR. 2. The respondent is a trade association established for the benefit of its members. It acts as the bargaining agent for and negotiates labor contracts on behalf of its members with certain labor unions. The association handles grievances and other administrative problems under the terms and conditions of any collective bargaining contract entered into on behalf of its members. The association has gathered and disseminated information to its respective members concerning the guarantees which are available in the roofing contracting business for new and replacement roofs and which are available and used in regard to waterproofing and dampproofing contracts. As a result of the conduct and activities of respondent and its members as described above, the acts and practices herein complained of are in or affect "commerce" within the meaning of the Federal Trade Commission Act, as amended, and respondent is subject to the jurisdiction of the Federal Trade Commission.

PAR. 3. On or about February 15, 1974, the members of the Inland Empire Roofing Contractors Association decided to modify the terms of guarantees then being offered with regard to waterproofing and dampproofing contracts. Some time between March 22, 1974 and April 19, 1974, officers and directors of said association acting within the scope of their authority and at the direction of the Inland Empire Roofing Contractors Association, met with members of the Seattle-based Roofing Contractors Association and discussed the terms of guarantees that would be offered by members of each respective association for waterproofing and dampproofing contracts. Some time after April 19, 1974, the Inland Empire Roofing Contractors Association adopted or proposed adopting an arrangement whereby no guarantees would be issued by its members for waterproofing or dampproofing work and that a two-year guarantee would be issued by its members for roofing work on all new and replacement roofs. On or about May 16, 1974, an agreement was reached by the members of the Inland Empire Roofing Contractors Association to the effect that no guarantees would be offered on waterproofing or dampproofing work and further that no guarantee for damage to roofs caused by certain wind conditions would be provided to customers of said members.

PAR. 4. The effects, among others, of the acts and practices alleged in Paragraph Three are as follows:

A. Terms of guarantees for new and replacement roofs have been fixed, stabilized or otherwise interfered with;

B. Competition among member roofing contractors in providing roofing services has been restrained, hindered, frustrated and/or foreclosed;

C. Customers of roofing services have been deprived of information, options and services pertinent to the selection of a roofer and the benefits of competition; and

D. Member roofers have been restrained in their ability to compete and to make alternative guarantee terms available to customers.

PAR. 5. The aforesaid acts, practices, and methods of competition of respondent constitute unfair methods of competition and unfair acts or practices in violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

Chairman Pertschuk did not participate.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Seattle Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure described in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Inland Empire Roofing Contractors Association is an unincorporated association organized, existing and doing business under and by virtue of the laws of the State of Washington, with its office and principal place of business located at East 130 Sprague Ave., in the City of Spokane, State of Washington.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

I

A. Definitions established for the purpose of the following order provisions are:

1. "Other related services" includes but is not limited to, repairing of roofs, inspecting of roofs, waterproofing and dampproofing of roofs, and estimating costs of repair or installation of roofs.
2. "Others not party hereto" means any individual, individual proprietorship, partnership, firm, corporation, association or any other form of legal or business entity.

II

A. *It is ordered,* That respondent Inland Empire Roofing Contractors Association, an unincorporated association, its successors and assigns, and its agents, representatives, and employees, directly or through any corporation, subsidiary, division or any other device, in connection with the advertising, offering for sale, sale and installation of new or replacement roofs or other related services in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

1. Entering into any contract, agreement, course of conduct, or understanding between itself and others not party hereto to fix, establish, stabilize, or maintain, the length or other term of any guarantee;
2. Entering into any contract, agreement, course of conduct, or understanding between itself and others not party hereto to fix, establish, stabilize or maintain any price or other term or condition of sale in connection with the sale and installation of new or replacement roofs or for performing other related services.

III

A. *It is further ordered,* That respondent Inland Empire Roofing Contractors Association, an unincorporated association, its successors and assigns, and its agents, representatives, and employees, directly or through any corporation, subsidiary, division or any other device, in connection with the advertising, offering for sale, sale and installation of new or replacement roofs or other related services in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

1. Urging, recommending, or suggesting that any of its members or any other person adopt or adhere to any particular guarantee or to any price or other term or condition of sale in connection with the sale and installation of new or replacement roofs or for performing other related services;
2. Adopting, adhering to, maintaining, enforcing or claiming any rights under any bylaw, rule, regulation, plan or program which limits in any way a member's right to give or offer a guarantee or any price or other term or condition of sale to any customer or prospective customer in connection with the sale or installation of a new or replacement roof or for performing other related services;
3. Investigating and/or policing a price or guarantee term charged or imposed by any member of the association or any other person in connection with the installation of new or replacement roofs.

IV

A. *It is further ordered,* That respondent Inland Empire Roofing Contractors Association shall within sixty (60) days after the date of service of this order, mail a copy to each of its existing members and to each person who was a member at any time from June 30, 1973 to date of service of this order, and furnish a copy of this order to each prospective member for a period of five (5) years after the date of service of this order.

B. *It is further ordered,* That respondent notify the Commission at least thirty (30) days prior to any proposed change in the respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation or association, the creation or dissolution of subsidiaries or any other change in the association which may affect compliance obligations arising out of the order.

C. *It is further ordered,* That the respondent herein shall within sixty (60) days after service on it of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

Chairman Pertschuk did not participate.

IN THE MATTER OF

FORD MOTOR COMPANY

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9001. Complaint, Dec. 10, 1974 — Decision, May 24, 1979

This consent order, among other things, requires a Dearborn, Mich. automobile manufacturer to cease, in connection with automobiles marketed by its Lincoln-Mercury Division, misrepresenting the fuel economy of any automobile or its superiority over competitive products; and the purpose, contents and results of automotive tests. Additionally, the firm is required to substantiate all claims regarding the structural strength, quietness, fuel economy and performance of its products, and maintain such substantiation for a three-year period.

Appearances

For the Commission: *Russell Hatchl, Mitchell Paul* and *Deborah Randall.*

For the respondent: *Robert L. Wald, Wald, Harkrader & Ross,* Washington, D.C. and *David R. Larrouy,* Dearborn, Mich.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Ford Motor Company, a corporation, hereinafter referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Ford Motor Company is a corporation, organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its executive office and principal place of business located at The American Road, Dearborn, Michigan.

PAR. 2. Respondent is now, and for some time last past has been, engaged in the manufacture, distribution, sale, and advertising of various products including automobiles.

PAR. 3. Respondent causes the said products, when sold, to be transported from its place of business in various States of the United States to purchasers located in various other States of the United States and in the District of Columbia. Respondent maintains, and at all times mentioned herein has maintained, a course of trade in said products in commerce. The volume of business in such commerce has been and is substantial.

PAR. 4. In the course and conduct of its said business, respondent has disseminated and caused the dissemination of advertisements concerning its aformentioned products including automobiles in commerce by means of advertisements printed in magazines and newspapers distributed by the mail and across state lines and transmitted by television stations located in various States of the United States and in the District of Columbia, having sufficient power to carry such broadcasts across state lines, for the purpose of inducing and which were likely to induce, directly or indirectly, the purchase of said products including automobiles.

PAR. 5. Among the advertisements so disseminated or caused to be disseminated by respondent are the advertisements attached as Exhibits A and B.

PAR. 6. Said Exhibits A and B and others substantially similar thereto contain one or more false, deceptive and misleading representations and fail to disclose facts which are material in the light of the representations contained therein. Therefore, the representations contained in said advertisements were, and are, deceptive and/or unfair.

PAR. 7. Said Exhibits A and B and others substantially similar thereto (hereinafter referred to as said advertisements) represent, directly or by implication, that the gasoline consumption rates specified in the advertisements approximate or equal the performance an ordinary driver can typically obtain from standard production model cars when taking long or cross-country trips.

PAR. 8. In truth and in fact, at the time respondent made the representations as alleged in Paragraph Seven respondent did not possess and rely upon a reasonable basis for making these representations. Therefore the said advertisements were, and are unfair and/or deceptive.

PAR. 9. Said Exhibits A and B and others substantially similar thereto represent, directly or by implication, that respondent had a reasonable basis for making, at the time they were made, the representations as alleged in Paragraph Seven.

PAR. 10. In truth and in fact, at the time respondent made the representations as alleged in Paragraph Nine respondent had no reasonable basis for making the representations as alleged in Paragraph Seven. Therefore, the said advertisements were, and are deceptive and/or unfair.

PAR. 11. Respondent failed to disclose in said advertisements that it had no evidence that any or all of the conditions under which the tests described in the advertisements were conducted approximated or equalled the conditions under which an ordinary driver would operate his automobile when taking long or cross country trips and that respondent had no evidence that would tend to show whether or not the conditions under which said tests were run were typical or atypical of conditions encountered by ordinary drivers.

PAR. 12. The facts set forth in Paragraph Eleven are material in light of the representations contained in said advertisements and their omission make these advertisements misleading in a material respect. Therefore, the said advertisements were, and are deceptive and/or unfair.

PAR. 13. In the course and conduct of the aforesaid business, and at all times mentioned herein, respondent Ford Motor Company has been and now is in substantial competition in commerce with corporations, firms, and individuals engaged in the sale and distribution of automobiles of the same general kind and nature as that sold by respondent.

PAR. 14. The use by respondent of the aforesaid unfair and/or deceptive statements, representations and practices has had, and now has, the capacity and tendency to mislead members of the consuming public into the purchase of substantial quantities of automobiles manufactured by respondent. Further, as a result thereof, substantial trade is being unfairly diverted to respondent from its competitors.

PAR. 15. The aforesaid acts and practices of respondent, as herein alleged, were and are all to the prejudice and injury of the public and of respondent's competitors and constituted, and now constitute, unfair or deceptive acts or practices in commerce and unfair methods of competition in commerce in violation of Section 5 of the Federal Trade Commission Act.

February 19th: [illegible] tested the highway mil[illegible]e of [illegible] Company's small cars. Today: the results.

EXHIBIT A

All 5 Ford Motor Company small cars got over 26 MPG.

The test.

At 7 15 AM, February 19th, five 1974 Ford Motor Company small cars (wheelbase under 112") were driven from Phoenix to Los Angeles to learn the kind of mileage they could get. The cars were a Ford Pinto, a Ford Maverick, a Ford Mustang II, a Mercury Comet and one of Mercury's Capris.

All the cars were regular production models with standard engines and transmissions. They weren't however, brand new. They had been broken in to simulate 6,000 miles of normal driving. All the cars used regular gas and had normal dealer preparation.

The drivers were not professionals. And they did not exceed 50 MPH.

In many respects the test was similar to one run on December 28th 1973, where five 1974 Ford LTD's delivered an average of 18.6 MPG.

The results.

These results show dramatically that these five small cars from Ford and Lincoln-Mercury did deliver economical gas mileage.

Of course, the mileage you will get depends on many factors: equipment, engine displacement, vehicle weight, local road conditions and your personal driving style. So the mileage you get may be less or even more than the figures quoted here.

Ford and Lincoln-Mercury dealers offer more types of gas-saving engines for small cars than anyone.

One of the most important factors determining small car mileage is a gas-saving engine. And Ford and Lincoln-Mercury dealers offer more types of gas-saving engines for small cars than anyone.

Two 4-cylinder engines. Some manufacturers of so-called "economy" cars don't even offer a 4-cylinder engine.

Ford Motor Company makes two different sizes of 4-cylinder engines. A 2.0 liter which was used in Pinto and Capri for this test, and the 2.3 liter used in Mustang II.

The 2.0 liter is the smallest displacement engine available today in an American made car from any major American manufacturer.

Ford Motor Company sells more 4-cylinder engines in American made cars than anyone else.

Two 6-cylinder engines. Ford and Lincoln-Mercury dealers offer two sizes of 6-cylinder engines for small cars: a 200 CID which was used in Maverick and Comet for this test, and an optional 250 CID.

Ford Motor Company's major competitor offers only one 6-cylinder engine for all of its car lines.

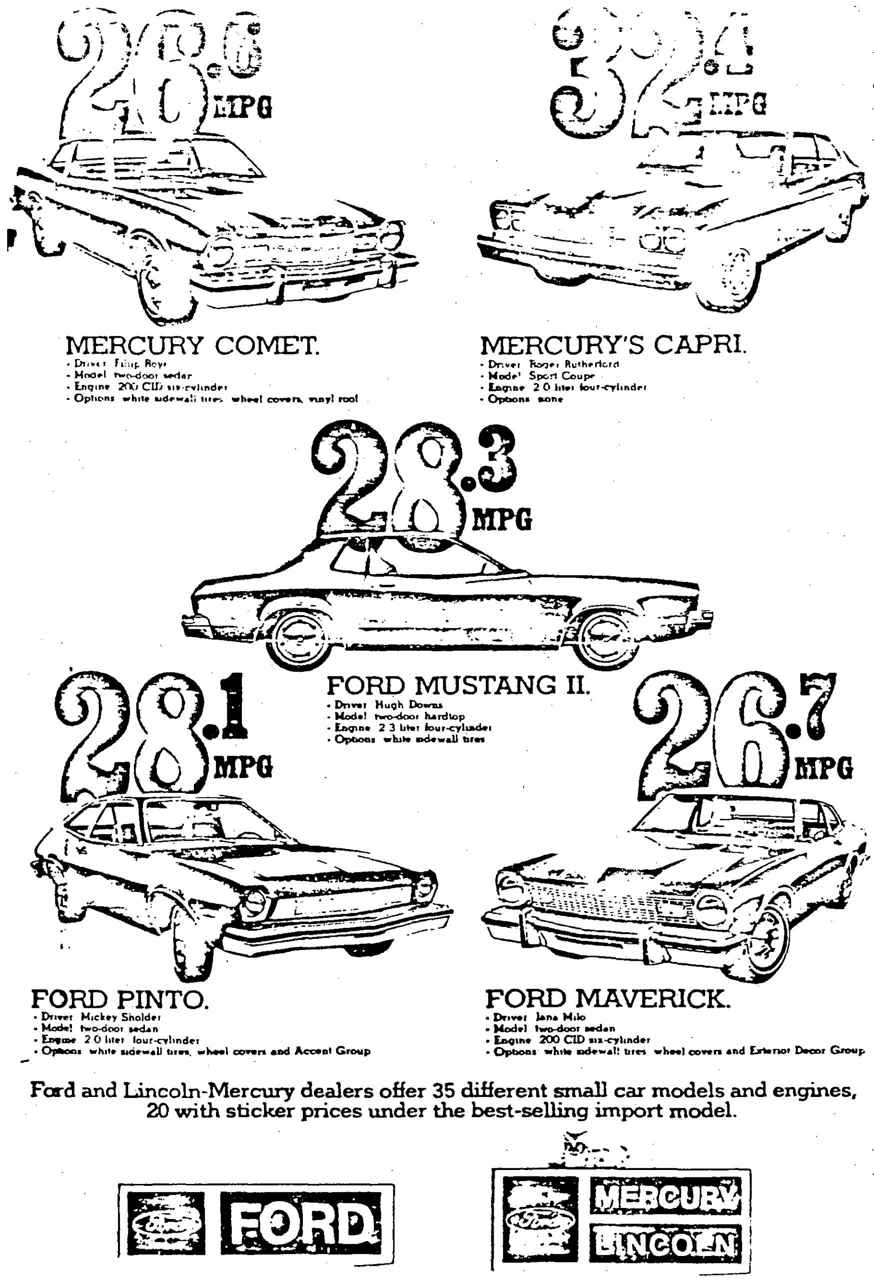
A V-6 engine. Ford Mustang II is the only car made by a major American manufacturer to offer an optional V-6.

Mercury's imported Capri offers an optional 2.8 liter V-6 engine at a cost thousands of dollars less than any other V-6 powered import.

An economy V-8 engine. Ford and Lincoln-Mercury dealers offer a 302 CID V-8 engine, the smallest displacement V-8 available from any major American manufacturer. It provides extra performance while still delivering good gas mileage.

Explanation of engine designations. CID OR LITER: the total volume, in cubic inches or liters (metric system) that the pistons displace in all the engine's cylinders.

FORD MOTOR COMPANY HAS MADE MORE SMALL CARS* THAN ANYONE ELSE IN THE WORLD (THAT INCLUDES VW, AMC, TOYOTA, GM, FIAT, DATSUN OR CHRYSLER)


32.4 MPG
MERCURY COMET.
- Model two-door sedan
- Engine 200 CID six-cylinder
- Options white sidewall tires, wheel covers, vinyl roof
MERCURY'S CAPRI.
- Driver Roger Rutherford
- Model Sport Coupe
- Engine 2.0 liter four-cylinder
- Options none
28.3 MPG
FORD MUSTANG II.
- Driver Hugh Downs
- Model two-door hardtop
- Engine 2.3 liter four-cylinder
- Options white sidewall tires
28.1 MPG
FORD PINTO.
- Driver Mickey Sholder
- Model two-door sedan
- Engine 2.0 liter four-cylinder
- Options white sidewall tires, wheel covers and Accent Group
26.7 MPG
FORD MAVERICK.
- Driver Jana Milo
- Model two-door sedan
- Engine 200 CID six-cylinder
- Options white sidewall tires, wheel covers and Exterior Decor Group
Ford and Lincoln-Mercury dealers offer 35 different small car models and engines, 20 with sticker prices under the best-selling import model.
FORD
MERCURY
LINCOLN

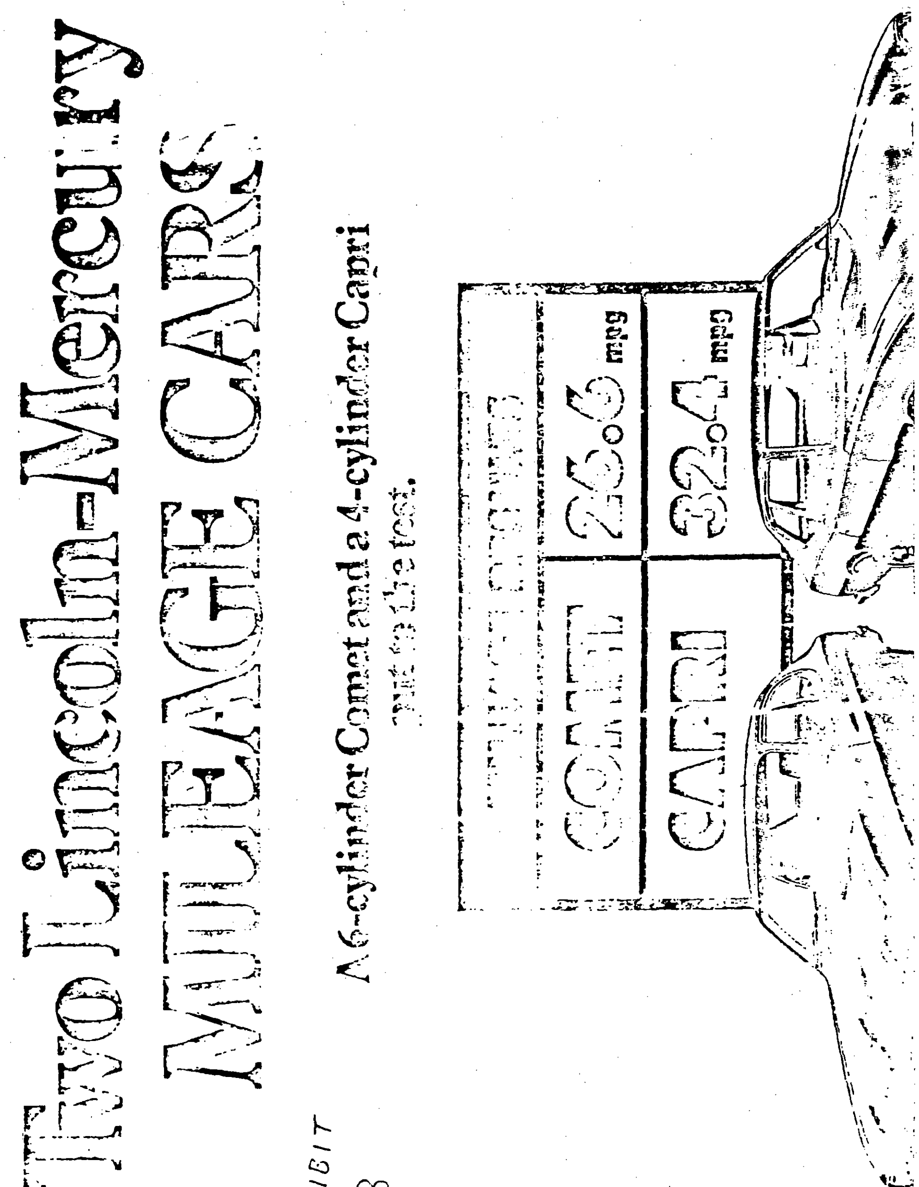

Two Lincoln-Mercury
MILEAGE CARS
A 6-cylinder Comet and a 4-cylinder Capri
put to the test.
COMET 26.6 mpg
CAPRI 32.4 mpg

EXHIBIT
B

February 19, 1974: In a 379 mile highway test through Arizona and California, supervised by General Environments Corporation, a Comet and a Capri with standard engines and transmissions delivered the kind of gas mileage you'd like to get. Each car was broken in the equivalent of 6,000 miles and driven by non-professional drivers, never exceeding 50 mph. You yourself might actually average less, or for that matter more! Because mileage varies according to maintenance, equipment, total weight, driving habits and road conditions. And no two drivers, or even cars, are exactly the same. Stop in at your Lincoln-Mercury dealer's Mileage Headquarters and see what kind of mileage you can get.

Lincoln-Mercury Division

WASHINGTON

LEE D. BUTLER, INC.
[illegible] 21ST STREET, N.W.
WASHINGTON, D.C.

SUBURBAN

DAVE PYLES LINCOLN MERCURY, INC.
[illegible] LITTLE RIVER TURNPIKE
ALEXANDRIA, VIRGINIA

O'BRIEN & ROHALL, INC.
[illegible] HIGHWAY
[illegible], VA.

BILL BOGLEY LINCOLN-MERCURY, INC.
7809 WISCONSIN AVENUE
BETHESDA, MARYLAND

B. M. WOODFIELD MERCURY
26501 RIDGE ROAD
DAMASCUS, MARYLAND

HERNDON MOTOR COMPANY, INC.
93 WASHINGTON AVENUE
HERNDON, VA.

TOM CURRO LINCOLN-MERCURY, INC.
123 27 WASHINGTON BLVD.
LAUREL, MARYLAND

JIM ECKELS LINCOLN-MERCURY, INC.
8389 CENTERVILLE ROAD
MANASSAS, VIRGINIA

WILSON POWELL LINCOLN-MERCURY, INC.
4700 BRANCH AVENUE
MARLOW HEIGHTS, MARYLAND

EAST-WEST LINCOLN-MERCURY, INC.
7591 ANNAPOLIS ROAD
LANDOVER HILLS, MARYLAND

THOMASSEN LINCOLN-MERCURY, INC.
1125 ROCKVILLE PIKE
ROCKVILLE, MARYLAND

SAFFORD LINCOLN-MERCURY
8507 COLESVILLE RD
SILVER SPRING, MARYLAND

CHERNER LINCOLN-MERCURY, INC.
8550 LEESBURG PIKE
TYSON'S CORNER, VIRGINIA

DECISION AND ORDER

The Commission having heretofore issued its complaint charging the respondent named in the caption hereof with violation of Section 5 of the Federal Trade Commission Act, as amended, and the respondent having been served with a copy of that complaint, together with a notice of contemplated relief; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Secretary of the Commission having thereafter withdrawn this matter from adjudication in accordance with Section 3.25(c) of its Rules; and

The Commission having considered the matter and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 3.25(f) of its Rules, the Commission hereby makes the following jurisdictional findings and enters the following order:

1. Respondent Ford Motor Company is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at The American Road, Dearborn, Michigan.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

It is ordered, That respondent, Ford Motor Company, its successors nd assigns, its officers, agents, representatives and employees, irectly or through any corporation, subsidiary, division or device, in nnection with the advertising, offering for sale, sale or distribuon, in or affecting commerce as "commerce" is defined in the deral Trade Commission Act, of automobiles marketed by the ncoln-Mercury Division, do forthwith cease and desist from:

1. Misrepresenting in any manner the fuel economy of any

automobile or the superiority of any automobile over competing products in terms of fuel economy.

2. Making any representations, directly or by implication, concerning the structural strength, quietness or fuel economy of such products or any part thereof, unless respondent possesses and relies upon a reasonable basis for such representations; provided that such a reasonable basis shall consist of competent and reliable scientific tests or other competent and reliable objective materials, including competent and reliable opinions of scientific, engineering or other experts who are qualified by professional training and experience to render competent judgments in such matters.

3. (a) Representing, directly or by implication, by reference to a test or tests, that the performance of any automobile has been tested either alone or in comparison with other automobiles unless such representation(s) accurately reflect the test results and unless the tests themselves are so devised and conducted as to substantiate each such representation concerning the featured tests.

(b) Misrepresenting in any manner the purpose, contents or conclusion of any test or tests relating to the performance of its automobiles.

For purposes of Paragraph 3(a) and 3(b) of this order, "test" shall include demonstrations, experiments, surveys, reports and studies.

4. Failing to maintain accurate records which may be inspected by Commission staff members upon reasonable notice:

(a) Which consist of documentation in support of any representation covered by this order included in advertising or sales promotional material disseminated by respondent, insofar as the advertising or sales promotional material is prepared, or is authorized and approved, by any person who is an officer or employee of respondent, or of any division or subdivision of respondent;

(b) Which provided the basis upon which respondent relied as of the time the representation covered by this Order was made; and

(c) Which shall be maintained by respondent for a period of three years from the date such advertising or sales promotional material was last disseminated by respondent or any division or subsidiary of respondent.

It is further ordered, That respondent shall forthwith distribute a copy of this order to its operating divisions involved in the advertising, promotion, distribution, or sale of automobiles.

It is further ordered, That respondent shall notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale result ing in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of this order.

It is further ordered, That respondent shall, within sixty (60) days after the effective date of this order, file with the Commission a report, in writing, signed by respondent, setting forth in detail the manner and form of its compliance with this order.

IN THE MATTER OF

RHINECHEM CORPORATION, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket 9116. Complaint, Aug. 23, 1978 — Decision, June 6, 1979

This consent order, among other things, requires a New York City manufacturer and seller of organic pigments to terminate all agreements providing for the acquisition of the Chemetron Corporation's organic pigments business; return all confidential documents exchanged during the negotiations; and provide the Commission with evidence of its compliance with these requirements. Additionally, respondent is required, until December 31, 1981, to furnish the Commission with 90-days' advance notice should the firm seek to acquire Chemetron's organic pigment business, or sell its own organic pigment business to Chemetron or Chemetron's corporate parent, Allegheny Ludlum Industries, Inc.

Appearances

For the Commission: *Glenn M. Fellman, Michael P. Waxman, John M. Peterson* and *Benita A. Sakin.*

For the respondents: *Thomas L. VanKirk, Buchanan, Ingersoll, Roderwald, Kyle & Buerger,* Washington, D.C. and *H. Blair White, Sidley & Austin,* Chicago, Ill.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondents, each subject to the jurisdiction of the Commission, have entered into a merger agreement which, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45; that said agreement constitutes a violation of Section 5 of the Federal Trade Commission Act, as amended; and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, pursuant to Section 11 of the Clayton Act, 15 U.S.C. 21, and Section 5(b), of the Federal Trade Commission Act, 15 U.S.C. 45(b), stating its charges as follows:

Definition

For purposes of this complaint the following definition shall apply:
Organic pigments - insoluble color particles characterized by a chemical composition which includes carbon rings or chains as the

basic part of their molecular structure and used to impart color to a variety of materials.

Rhinechem Corporation

1. Rhinechem Corporation (Rhinechem) is a corporation organized under the laws of the State of Delaware, with its principal place of business at 425 Park Ave., New York, New York.

2. Rhinechem is a wholly-owned subsidiary of Bayer International Finance N.A. which in turn is a wholly-owned subsidiary of Bayer Aktiengesellschaft (Bayer), a West German corporation with headquarters in Leverkusen, West Germany.

3. Bayer manufactures and sells organic pigments and organic pigment formulations throughout the world.

4. Rhinechem, through its wholly-owned subsidiaries, Mobay Chemical Corporation (Mobay) and Harmon Colors Corporation (Harmon) manufactures and sells organic pigments and organic pigment formulations in the United States.

5. In its fiscal year ended December 31, 1977, Rhinechem had total sales of approximately $1,329,979,000 of which domestic sales accounted for $1,151,574,000; Mobay had total commercial sales of $622,087,000; and Harmon had total commercial sales of $21,428,000.

6. Harmon is the eighth largest manufacturer of organic pigments in the United States.

7. Harmon is now and for many years has been a member of the Dry Colors Manufacturers Association (DCMA) which is a trade association made up of the major manufacturers of organic and inorganic pigments.

Chemetron Corporation

8. Chemetron Corporation (Chemetron) is a corporation organized under the laws of the State of Delaware, with its principal place of business at 111 E. Wacker Drive, Chicago, Illinois.

9. Chemetron is a wholly-owned subsidiary of Allegheny Ludlum Industries (Allegheny), a corporation organized under the laws of the Commonwealth of Pennsylvania, with its principal place of business at 2700 Two Oliver Plaza, Pittsburgh, Pennsylvania.

10. Chemetron through its unincorporated Pigments Division (CPD) produces organic pigments and sells said organic pigments throughout the United States.

11. In its fiscal year ended January 1, 1978, Chemetron had net sales of approximately $493,906,000, while CPD's net sales were approximately $51,784,000.

12. CPD is the third largest manufacturer of organic pigments in the United States.

13. Chemetron is now and for many years has been a member of the Dry Colors Manufacturers Association (DCMA).

Jurisdiction

14. At all times relevant herein Rhinechem and Chemetron have been engaged in the manufacture and sale of organic pigments in interstate commerce and are engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. 12, and each is a corporation whose business is in or affects commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

The Merger Agreement

15. On or about June 12, 1978, Rhinechem and Allegheny entered into an agreement in principle which provides, *inter alia,* for the acquisition by Rhinechem of the assets of Chemetron's Pigment Division.

Trade and Commerce

16. The relevant line of commerce is the manufacture and sale of organic pigments and submarkets thereof.

17. A relevant section of the country or geographic market is the entire United States.

18. The manufacture and sale of organic pigments is concentrated, with the combined market share of the four largest manufacturers estimated to be approximately 51%.

19. Barriers to entry into the manufacture and sale of organic pigments are substantial.

Actual Competition

20. Rhinechem and Chemetron are and have been for many years actual competitors of each other in the manufacture and sale of organic pigments and submarkets thereof and actual competitors of others engaged in the manufacture and sale of organic pigments and submarkets thereof throughout the United States.

21. In 1977, Rhinechem accounted for approximately 6.73% of United States production and sale of organic pigments and Chemetron's Pigment Division accounted for approximately 11.77% thereof.

Effects; Violations Charged

22. The effects of the proposed acquisition may be to substantially lessen competition or tend to create a monopoly in the relevant market in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, in the following ways, among others:

(a) actual competition between Rhinechem and Chemetron in the manufacture and sale of organic pigments and submarkets thereof will be eliminated;
(b) actual competition between competitors generally in the manufacture and sale of organic pigments and submarkets thereof may be lessened;
(c) Chemetron's Pigment Division will be eliminated as an actual substantial independent competitor in the manufacture and sale of organic pigments and sub-markets thereof;
(d) the merger will result in increased concentration in the manufacture and sale of organic pigments and diminishing possibilities for eventual deconcentration; and
(e) mergers or acquisitions between other organic pigment manufacturers may be fostered, thus causing a further substantial lessening of competition and tendency toward monopoly in the manufacture and sale of organic pigments.

Decision and Order

The Commission having heretofore issued its complaint charging the Rhinechem Corporation (hereinafter "respondent") named in the caption hereof with violation of Section 5 of the Federal Trade Commission Act, as amended, and Section 7 of the Clayton act, and the respondent having been served with a copy of that complaint, together with a notice of contemplated relief; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Secretary of the Commission having thereafter withdrawn this matter from adjudication in accordance with Section 3.25(c) of its Rules; and

The Commission having considered the matter and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 3.25(f) of its Rules, the Commission hereby makes the following jurisdictional findings and enters the following order:

1. Respondent Rhinechem Corporation is a corporation, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 425 Park Ave., in the City of New York, State of New York.
2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

Definitions

For purposes of this order the following definition shall apply:

Organic pigments means insoluble color particles characterized by a chemical composition which includes carbon rings or chains as the basic part of their molecular structure and used to impart color to a variety of materials.

I

It is ordered, That Rhinechem forthwith terminate all agreements which provided for the acquisition of the organic pigments business of Chemetron Corporation by a subsidiary of Rhinechem and provide evidence that all such agreements have been terminated and that all confidential documents provided to Rhinechem by Allegheny Ludlum Industries, Inc., and Chemetron Corporation in connection with the merger agreement have been returned or destroyed. Nothing herein contained shall relieve Rhinechem from any obligations of confidentiality imposed by agreement between the parties.

II

It is further ordered, That through December 31, 1981, Rhinechem, its successors or assigns, shall not acquire, either directly or indirectly, any or all of the organic pigments business of Chemetron Corporation nor shall it sell any or all of its organic pigments business to Allegheny Ludlum Industries, Inc., or Chemetron Corporation, whether represented by securities or assets, until ninety (90) days following receipt by the Director of the Bureau of

Competition of the Federal Trade Commission of written notice of the proposed acquisition or merger, such written notice to be similar in form and content to the notice required under Section 7A of the Clayton Act and the premerger notification rules promulgated thereunder and shall specifically refer to this order. (This provision shall not prohibit sales of organic pigments or other transactions between Rhinechem and Chemetron Corporation in the ordinary course of business.) If within ninety (90) days of receipt by the Director of such notice the Commission issues an administrative complaint challenging the proposed acquisition or merger, such proposed acquisition or merger shall not be consummated, nor shall any steps be taken to effectuate such proposed acquisition or merger until the administrative complaint issued by the Commission is dismissed by the Commission, until a final order as defined in 15 U.S.C. 21, 45 is entered or until a consent order is entered and served upon Rhinechem in the administrative proceeding. If within the aforesaid ninety (90) days the Bureau of Competition receives any written position papers from Rhinechem and the Bureau recommends issuance of a complaint, the Bureau shall promptly forward to the Commission such papers together with the written notice submitted to the Bureau Director. In the event that within ninety (90) days of the Director's receipt of such notice the Commission issues an administrative complaint challenging the proposed acquisition or merger, the Bureau of Competition shall exert its best efforts to complete the administrative proceeding in an expedited manner.

III

It is further ordered, That Rhinechem shall notify the Commission at least thirty (30) days prior to any proposed corporate change such as dissolution, assignment or sale, resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change which may affect compliance obligations arising out of this order.

IV

It is further ordered, That Rhinechem shall within sixty (60) days after service upon it of this order file with the Commission a written report setting forth in detail the manner and form in which it has complied with this order.

IN THE MATTER OF

APPLIANCE DEALERS COOPERATIVE, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2969. Complaint, June 7, 1979 — Decision, June 7, 1979

This consent order, among other things, requires a Newark, N.J. appliance dealers cooperative, its executive director, 22 member companies, and five affiliated firms to cease harassing, intimidating or otherwise attempting to control or interfere with retailers' resale pricing; advertising; sale and distribution of consumer products; selection of customers; or their right to locate and operate businesses in any geographic area. The cooperative is further required to supply its members, on an equal and timely basis, with all relevant information relating to its purchase and sale of merchandise; and cause its by-laws to be adjusted so as to be consistent with the terms of the order.

Appearances

For the Commission: *Alfred J. Ferrogari* and *Henry R. Whitlock.*

For the respondents: *Basil J. Mezines, Stein, Mitchell & Mezines,* Washington, D.C., *Ephraim Frank Schwartz,* Passaic, N.J., *Marvin S. Goldklang, Cahill, Gordon & Reindell,* New York City and *Gerard C. Sims, Jr.* and *Allan Raven, Raven, Davis & Sweet,* Adison, N.J.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that the parties named in the caption hereof, hereinafter more particularly described and designated as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Appliance Dealers Cooperative (hereinafter referred to as ADC) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. ADC maintains its home office and principal place of business at 84 Lockwood St., Newark, New Jersey. ADC operates as a buying cooperative for its shareholder-members, supplying these members with a variety of consumer appliances and products. Its members are corporate and non-corporate business enterprises which are engaged primarily in the retail sale of consumer appliances and products.

PAR. 2. Respondent Murray Gidseg (hereinafter sometimes referred to as Executive Director) is, and has been, for some time past, Executive Director of ADC and as such is, and has been, the chief executive officer of the corporation with all of the general powers and duties which are usually vested in the office of president of a corporation. As such, Murray Gidseg has charge of the administrative activities of ADC, helps conduct and actually participates in the meetings of the members of ADC and cooperates and acts together with other respondents to formulate, direct and control the policies, acts and practices of ADC, all in pursuance and furtherance of the establishing carrying out and maintaining of the policies, acts and practices hereinafter alleged. The business address of Murray Gidseg is the same as that of respondent ADC.

PAR. 3. The authority for formulation and management of policy with respect to all matters affecting the business of ADC is, and has been, vested in the ADC Board of Directors. The Board of Directors has at all times consisted of persons drawn from the companies who are members of ADC. From the inception of ADC in April 1972 until May 1974, all members of ADC were represented on its Board of Directors. From May 1974 until May 1975 one member was excluded from the ADC Board of Directors. From May 1975 until the next election of Board members in 1976, three additional members were excluded from the ADC Board of Directors. Except to the extent that decision making authority has been delegated by the Board of Directors to others, the Board has general overall supervision of all aspects of the business of ADC.

PAR. 4. Historically, since the inception of ADC in 1972, the Board of Directors has delegated much of its authority for formulation and management of policy to the Executive Director and certain officers and employees of the member companies who represent their respective firms at ADC membership meetings and who also serve on various ADC committees. Said persons, together with the Board of Directors and the Executive Director, formulated, directed and controlled the policies and activities of ADC and in doing so expressly or impliedly authorized, performed, adopted, acquiesced in or affirmed the policies, acts and practices herein alleged.

PAR. 5. Respondents Ace Electronic Service Co., Inc. (hereinafter Ace) and Solar Appliance Centers, Inc. (hereinafter Solar) are corporations organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Ace maintains its home office and principal place of business at 69 Highway 35, Neptune City, New Jersey. Solar maintains its home office and principal place of business at 2114 Route 88, Bricktown, New Jersey.

PAR. 6. Respondent Ajay Appliance Sales & Service, Inc. (hereinafter Ajay) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Ajay maintains its home office and principal place of business at 1021 Route 37 West, Toms River, New Jersey.

PAR. 7. Respondent Apex Appliance Distributors, Inc. (hereinafter Apex) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Apex maintains its home office and principal place of business at 700 Rahway Ave., Elizabeth, New Jersey.

PAR. 8. Respondent Bell Appliance Co., Inc. (hereinafter Bell) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Bell maintains its home office and principal place of business at Highway 22, Union, New Jersey.

PAR. 9. Respondent Paul Bergman is an individual trading and doing business as Brown's Appliance Co. (hereinafter Brown's) with its home office and principal place of business located at 276 Main St., Paterson, New Jersey.

PAR. 10. Respondent Charles Stein is an individual trading and doing business as Economy Stove & Plumbing Supply Co. (hereinafter Economy) with its home office and principal place of business located at 1047 Elizabeth Ave., Elizabeth, New Jersey.

PAR. 11. Respondent Flynn Appliances, Inc. (hereinafter Flynn) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Flynn maintains its home office and principal place of business at 44 Grand Ave., Englewood, New Jersey.

PAR. 12. Respondent Frank Schwartz is an individual trading and doing business as Franks Sales & Service Co. (hereinafter Franks) with its home office and principal place of business located at 739 Main Ave., Passaic, New Jersey.

PAR. 13. Respondents Goldklang's Appliance City, Inc. (hereinafter Goldklang's) and Town Appliance, Inc. (hereinafter Town), are corporations organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Goldklang's maintains its home office and principal place of business at 462 Broadway, Bayonne, New Jersey. Town maintains its home office and principal place of business at Route 46, Rockaway, New Jersey.

PAR. 14. Respondent Harvey's of New Milford, Inc. (hereinafter Harvey's) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Harvey's

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maintains its home office and principal place of business at 690 River Road, New Milford, New Jersey.

PAR. 15. Respondent Karl's Sales & Service Co., Inc. (hereinafter Karl's) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Karl's maintains its home office and principal place of business at 111 Washington Ave., Belleville, New Jersey.

PAR. 16. Respondent Keystone Appliance Co., Inc. (hereinafter Keystone) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Keystone maintains its home office and principal place of business at 4237 Bergen Turnpike, North Bergen, New Jersey.

PAR. 17. Respondent Lichtman Bros. Inc. (hereinafter Lichtman) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Lichtman maintains its home office and principal place of business at 101-105 Smith St., Perth Amboy, New Jersey.

PAR. 18. Respondent Mrs. G. Inc. (hereinafter Mrs. G.) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Mrs. G. maintains its home office and principal place of business at 2960 Brunswick Pike, Trenton, New Jersey.

PAR. 19. Respondent Paul's Home Furnishings Co., Inc. (hereinafter Paul's) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Paul's maintains its home office and principal place of business at 121 New York Ave., Newark, New Jersey.

PAR. 20. Respondent Rooney Appliance, Inc. (hereinafter Rooney) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Rooney maintains its home office and principal place of business at 500 Market St., Saddle Brook, New Jersey.

PAR. 21. Respondent Schenck Appliance Corporation (hereinafter Schenck) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Schenck maintains its home office and principal place of business at Route 88 and Laurelton Circle, Bricktown, New Jersey.

PAR. 22. Respondent Summerton Appliance, Inc. (hereinafter Summerton) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Summerton maintains its home office and principal place of business at 300 Route 9, Englishtown, New Jersey.

PAR. 23. Respondent Les Turchin, Inc. (hereinafter Les Turchin) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Les Turchin maintains its home office and principal place of business at 98–100 Albany St., New Brunswick, New Jersey.

PAR. 24. Respondent Tru-Home Sales Co. Inc. (hereinafter Tru-Home) is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Tru-Home maintains its home office and principal place of business at 321–16th Ave., Newark, New Jersey.

PAR. 25. Respondents Turchin's Department Stores, Inc. (hereinafter Turchin's) and Turchin's-Rex, Inc. (hereinafter Turchin's-Rex) are corporations organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Turchin's maintains it home office and principal place of business at 116 N. Wood Ave., Linden, New Jersey. Turchin's-Rex maintains its home office and principal place of business at 2385 Kennedy Boulevard, Jersey City, New Jersey.

PAR. 26. Respondents Uneeda Appliance Co., Inc. (hereinafter Uneeda), Uneeda Brook's Inc. (hereinafter Uneeda Brook's), and Uneeda Appliance Company of Bayonne, Inc. (hereinafter Uneeda Bayonne) are corporations organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Uneeda maintains its home office and principal place of business at 2973 Kennedy Boulevard, Jersey City, New Jersey. Uneeda Brook's maintains its home office and principal place of business at 9 West Main Street, Somerville, New Jersey. Uneeda Bayonne maintains its home office and principal place of business at 432 Broadway, Bayonne, New Jersey.

PAR. 27. Respondents Ace, Solar, Ajay, Apex, Bell, Brown's, Economy, Flynn, Franks, Goldklang's, Town, Harvey's, Karl's, Keystone, Lichtman, Mrs. G., Paul's, Rooney, Schenck, Summerton, Les Turchin, Tru-Home, Turchin's, Turchin's-Rex, Uneeda, Uneeda Brook's, Uneeda Bayonne (sometimes referred to as "respondent retailers") are now, and for some time past, have been engaged in the purchasing, offering for sale, sale and distribution of consumer appliances and products to the public at retail.

With the exception of Solar, Town, Turchin's-Rex, Uneeda Brook's and Uneeda Bayonne, (hereinafter sometimes referred to as respondent non-members) each of the remaining respondent retailers is, and has been, for some time past, a member of respondent ADC (hereinafter sometimes referred to as respondent members). Respondent non-members are affiliated with certain of respondent members through common ownership or otherwise. Respondent members purchase a substantial amount of consumer appliances and products from respondent ADC. Certain respondent members resell or transfer a substantial amount of said consumer appliances and products to their affiliated respondent non-members. In that manner respondent non-members derive many of the benefits of membership in respondent ADC.

PAR. 28. In the course and conduct of their respective businesses, various respondent retailers purchase for resale a substantial amount of consumer appliances and products from suppliers located in various States of the United States. Such respondents cause these products, when purchased, to be transported from the place of manufacture, storage or purchase in various States of the United States across state lines to their places of business. In the further course of their respective businesses, such respondents cause and for some time past have caused, said consumer appliances and products, when sold by them, to be shipped from their places of business located in the State of New Jersey to customers, many of whom are located in the States of the United States other than the states where said respondents' businesses are located and states other than the states where said products were originally manufactured, stored or purchased. Such respondent retailers are and were, during the several years past, engaged in a substantial course of trade in consumer appliances and products in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act.

PAR. 29. Except to the extent that competition has been hampered, restrained, lessened or restricted by reason of the practices hereinafter described, each of the respondent retailers described in Paragraph Twenty-Seven hereof is, and has been, in substantial competition with one or more of the other respondent retailers therein described and with other retailers of consumer appliances and products.

PAR. 30. In the course and conduct of its business, as aforesaid, respondent ADC purchases for resale a substantial amount of consumer appliances and products from suppliers located in various States of the United States. Respondent ADC causes these products, when purchased by it, to be transported from the place of manufacture, storage or purchase in various States of the United States across state lines to its place of business. In the course and conduct of its business, respondent ADC has caused said consumer appliances and products, when sold by it, to be shipped from its place of business located in the State of New Jersey to purchasers located in other States of the United States.

In the course and conduct of its business, as aforesaid, respondent

ADC has caused checks, bills, invoices, letters and other documents to be mailed through the facilities of the United States mail, from its place of business located in the State of New Jersey to purchasers located in other States of the United States.

Accordingly, respondent ADC has maintained, and now maintains a substantial course of trade in consumer appliances and products in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act.

PAR. 31. For several years past, respondent ADC, respondent Executive Director and certain respondent retailers have been, and are, engaged in unfair acts and practices and unfair methods of competition in or affecting commerce, as herein described, which have the purpose, tendency and effect of lessening, restricting and suppressing competition among and between said respondent retailers, and among and between said respondent retailers and others, in the offering for sale, sale and distribution of consumer appliances and products.

PAR. 32. In the course and conduct of its business, respondent ADC, acting through respondent Executive Director and various ADC committees with the cooperation and/or acquiescence of the majority of respondent members, engaged in the following acts and practices:

(a) Respondent Executive Director and representatives of various respondent members acting as ADC committees and serving as common agents of all respondents have met with, and continue to meet with, suppliers of ADC for the purpose of ascertaining and negotiating the prices, terms and conditions of sale of consumer appliances and products offered by said suppliers. Subsequent to said discussions, regular meetings of respondent members are held under the auspices of ADC at which respondent Executive Director and representatives of various respondent members acting as ADC committees and serving as common agents of all respondents, relate to, and discuss with respondent members, the prices, terms and conditions of sale which they obtained from suppliers as well as their own suggestions and wishes with respect to the pricing, marketing and sales of said products by respondent retailers. Further suggestions and directions with respect to the pricing, marketing and sale of said products are communicated to respondent retailers by respondent ADC through the medium of news bulletins which are written by respondent Executive Director. At the ADC meetings and in the news bulletins, statements, admonitions, suggestions and threats of fines and penalties are made by respondent Executive Director and representatives of various respondent members acting as ADC committees, which are designed to induce and persuade, and did induce and persuade, the respondent retailers named herein to comply with the suggestions, wishes and directives made with respect to the pricing, marketing and sale of consumer appliances and products by said respondent retailers.

(b) Respondent ADC, with the knowledge, consent and approval of respondent Executive Director and the majority of respondent members, has, with regard to certain consumer appliances and products, withheld and continues to withhold from respondent retailers, knowledge of the amounts of certain rebates or allowances due them from respondent ADC for purchases made from, or through ADC, thus making it difficult or impossible for respondent retailers to determine their net cost for those certain items at the time of purchase. Cost is a significant factor in pricing merchandise for resale, thus, the purpose and effect of the "undisclosed holdback" practice is to prevent, discourage or inhibit respondent retailers from lowering their resale price by all or part of the amount of the undisclosed holdback and thus establish, maintain, raise, tamper with, control or stabilize the prices at which said products are advertised, offered for sale, or sold by respondent retailers. Additionally, the same undisclosed holdback practice has the effect of preventing, discouraging or inhibiting the resale of said products by respondent retailers to other retailers, a practice known as transshipping.

PAR. 33. Pursuant to, and by means of the acts and practices described in Paragraph Thirty-Two (a) and (b) above, respondent ADC, acting through respondent Executive Director, various committees of ADC, and certain respondent members performed and did persuade, induce and coerce other respondent members and respondent retailers to acquiesce in the performance of unlawful acts and practices among which are the following:

1. Maintain, establish, raise, tamper with or stabilize the prices at which certain consumer appliances and products are advertised, offered for sale or sold by respondent retailers.

2. Prevent, limit or inhibit respondent retailers from reselling certain consumer appliances and products purchased from respondent ADC, to other retail establishments, a practice commonly known as transshipping.

3. Refrain from locating and operating retail stores for the sale of consumer appliances and products in the geographic area or territory which is occupied and serviced by another respondent retailer.

4. For the purpose of effectuating the unlawful acts and practices

herinbefore described: harass, intimidate or coerce certain respondent retailers not conforming to the agreements or understandings herinbefore described through the use or threat of; fines, penalties, price discriminations, refusals to deal, suspension or termination of membership in ADC, refusal or failure to make timely payment of debts or obligations owing to members or resigning members of ADC, removal or exclusion of members of ADC from membership on or participation in, the activities of the Board of Directors, committees or subgroups of ADC, discriminatory treatment of members of ADC, failure to provide full and fair prior notice of all meetings which any member of ADC was permitted to attend and failure to provide members of ADC with an opportunity to attend and participate in such meetings.

PAR. 34. The acts, practices and methods of competition engaged in, followed, approved or acquiesced in by respondents, as hereinabove alleged, have the purpose, tendency and effect of hindering, lessening and restraining price and other competition between and among respondent retailers and between and among respondent retailers and other retailers, in the offering for sale, sale and distribution of consumer appliances and products.

PAR. 35. The acts, practices and methods of competition of respondents and the adverse competitive effects resulting therefrom as hereinabove set forth, are to the injury and prejudice of the public and of respondents' competitors and thus constitute unfair acts and practices and unfair methods of competition in or affecting commerce within the intent and meaning of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the New York Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to § 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Proposed respondent Appliance Dealers Cooperative is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey with its home office and principal place of business located at 84 Lockwood St., Newark, New Jersey.

Proposed respondent Murray Gidseg is Executive Director of Appliance Dealers Cooperative and as such is the chief executive officer of the corporation. He cooperates and acts together with other respondents to formulate, direct and control the policies, acts and practices of said corporation, and his address is the same as that of said corporation.

Proposed respondents Ace Electronic Service Co., Inc. (hereinafter Ace) and Solar Appliance Centers, Inc. (hereinafter Solar) are corporations organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Ace maintains its home office and principal place of business at 69 Highway 35, Neptune City, New Jersey. Solar maintains its home office and principal place of business at 2114 Route 88, Bricktown, New Jersey.

Proposed respondent Ajay Appliance Sales & Service, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 1021 Route 37 West, Toms River, New Jersey.

Proposed respondent Apex Appliance Distributors, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 700 Rahway Ave., Elizabeth, New Jersey.

Proposed respondent Bell Appliance Co., Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at Highway 22, Union, New Jersey.

Proposed respondent Paul Bergman is an individual trading and doing business as Brown's Appliance Co. with its home office and principal place of business located at 276 Main St., Paterson, New Jersey.

Proposed respondent Charles Stein is an individual trading and doing business as Economy Stove & Plumbing Supply Co. with its home office and principal place of business located at 1047 Elizabeth Ave., Elizabeth, New Jersey.

Proposed respondent Flynn Appliances, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 44 Grand Ave., Englewood, New Jersey.

Proposed respondent Frank Schwartz is an individual trading and doing business as Franks Sales & Service Co. with its home office and principal place of business located at 739 Main Ave., Passaic, New Jersey.

Proposed respondents Goldklang's Appliance City, Inc. (hereinafter Goldklang's) and Town Appliance, Inc. (hereinafter Town), are corporations organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Goldklang's maintains its home office and principal place of business at 462 Broadway, Bayonne, New Jersey. Town maintains its home office and principal place of business at Route 46, Rockaway, New Jersey.

Proposed respondent Harvey's of New Milford, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 690 River Road, New Milford, New Jersey.

Proposed respondent Karl's Sales & Service Co., Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 111 Washington Ave., Belleville, New Jersey.

Proposed respondent Keystone Appliance Co., Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 4237 Bergen Turnpike, North Bergen, New Jersey.

Proposed respondent Lichtman Bros. Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 101-105 Smith St., Perth Amboy, New Jersey.

Proposed respondent Mrs. G. Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 2960 Brunswick Pike, Trenton, New Jersey.

Proposed respondent Paul's Home Furnishings Co., Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 121 New York Ave., Newark, New Jersey.

Proposed respondent Rooney Appliance, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 500 Market St., Saddle Brook, New Jersey.

Proposed respondent Schenck Appliance Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at Route 88 and Laurelton Circle, Bricktown, New Jersey.

Proposed respondent Summerton Appliance, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 300 Route 9, Englishtown, New Jersey.

Proposed respondent Les Turchin, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 98-100 Albany St., New Brunswick, New Jersey.

Proposed respondent Tru-Home Sales Co. Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its home office and principal place of business at 321-16th Ave., Newark, New Jersey.

Proposed respondents Turchin's Department Stores, Inc. (hereinafter Turchin's) and Turchin's-Rex, Inc. (hereinafter Turchin's-Rex) are corporations organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Turchin's maintains its home office and principal place of business at 116 N. Wood Ave., Linden, New Jersey. Turchin's-Rex maintains its home office and principal place of business at 2385 Kennedy Boulevard, Jersey City, New Jersey.

Proposed respondents Uneeda Appliance Co., Inc. (hereinafter Uneeda), Uneeda Brook's, Inc. (hereinafter Uneeda Brook's) and Uneeda Appliance Company of Bayonne, Inc. (hereinafter Uneeda

Bayonne) are corporations organized, existing and doing business under and by virtue of the laws of the State of New Jersey. Uneeda maintains its home office and principal place of business at 2973 Kennedy Boulevard, Jersey City, New Jersey. Uneeda Brook's maintains its home office and principal place of business at 9 West Main St., Somerville, New Jersey. Uneeda Bayonne maintains its home office and principal place of business at 432 Broadway, Bayonne, New Jersey.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

I

It is ordered, That respondent Appliance Dealers Cooperative, a corporation, (hereinafter referred to as ADC) and respondent Murray Gidseg, individually and as Executive Director of ADC and said respondents' agents, representatives, employees, successors and assigns, directly or indirectly, through any corporate or other device in connection with the advertising, offering for sale, sale or distribution of consumer appliances and products in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, cease and desist from either individually doing, engaging in or performing any of the following acts, practices or policies or entering into, carrying out, cooperating or acquiescing in any common course of action, understanding, agreement or combination, whether express or implied, between said respondents or between any one or more of them and any other person or firm to do or perform any of the following:

1. Establish, tamper with, maintain, raise, stabilize or control the prices at which consumer appliances and products may be advertised, offered for sale or sold by any retailer.
2. Restrict, limit or otherwise interfere with the right of any retailer of consumer appliances and products to sell such products to any other person or firm.
3. Agree with any other person or firm to refuse to resell consumer appliances and products to any member of ADC unless the member is approved, authorized or franchised by suppliers to receive their merchandise.
4. Restrict, limit or otherwise interfere with the right of any

retailer to locate and operate retail stores in any geographic area or territory.

5. Harass, intimidate, coerce or otherwise interfere with any person or firm if an actual or potential effect of such conduct would be to cause or permit any of the acts, practices or policies prohibited by paragraphs one (1) through four (4) of this order.

6. Knowingly withhold or hold back from members or other customers of ADC any purchase price information or any information relating to the amounts of rebates, allowances or discounts due said members or other customers of ADC for merchandise purchased from or through ADC, or take or withhold any other action which has, or may have, the effect of impeding or preventing members or other customers of ADC from determining their net cost for consumer appliances and products at the time of purchase.

7. Communicate, circulate or exchange any information or material which has the purpose or effect of causing any of the acts, practices or policies prohibited by paragraphs one (1) through six (6) of this order.

II

It is further ordered, That Ace Electronic Service Co., Inc., Solar Appliance Centers, Inc., Ajay Appliance Sales & Service, Inc., Apex Appliance Distributors, Inc., Bell Appliance Co., Inc., Paul Bergman an individual trading and doing business as Brown's Appliance Co., Charles Stein an individual trading and doing business as Economy Stove & Plumbing Supply Co., Flynn Appliances, Inc., Frank Schwartz an individual trading and doing business as Franks Sales & Service Co., Goldklang's Appliance City, Inc., Harvey's of New Milford, Inc., Karl's Sales & Service Co., Inc., Keystone Appliance Co., Inc., Lichtman Bros. Inc., Mrs. G. Inc., Paul's Home Furnishings Co., Inc., Town Appliance, Inc., Rooney Appliance, Inc., Schenck Appliance Corporation, Summerton Appliance, Inc., Les Turchin, Inc., Tru-Home Sales Co. Inc., Turchin's Department Stores, Inc., Turchin's-Rex, Inc., Uneeda Appliance Co., Inc., Uneeda Brook's, Inc., Uneeda Appliance Company of Bayonne, Inc. (hereinafter referred to as respondent retailers) and said respondent retailers' successors, assigns, officers, representatives, agents and employees, directly or through any corporation, subsidiary, division, or any other device, in connection with the offering for sale, sale or distribution of consumer appliances and products in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, shall not, either individually or collectively:

Engage in, carry out, cooperate, or acquiesce in any act, practice or policy or any common course of action, understanding, agreement or combination between any two or more of said respondent retailers or between any one or more of them and respondent ADC or respondent Murray Gidseg, their representatives, agents, designees, successors and assigns, if an effect would be to restrict, interfere, or tamper with the purchase, advertising, pricing, offering for sale, sale or distribution of consumer appliances and products, the selection of customers, or the location of places of business by any person or firm, or between any one or more of said respondent retailers and any other person or firm, if an effect would be to restrict, interfere, or tamper with the purchase, advertising, or pricing of consumer appliances and products, or the location of places of business by any person or firm.

III

It is further ordered, That respondent ADC, either directly or through its representatives, designees, successors and assigns, shall disclose to ADC members on an equal and timely basis all material matters considered and actions taken at all board, committee, membership and subgroup meetings or by the membership, or any board, committee or subgroup which affect, or may affect, the business of ADC including, without limitation, all information relating to the purchase or sale by ADC of consumer appliances and products purchased or to be purchased by or on behalf of ADC, its agents, representatives or designees.

IV

It is further ordered, That respondent ADC, either directly or through its representatives, designees, successors and assigns, shall provide adequate and equal prior notice to each ADC member, of all meetings (except as to meetings of committees or subgroups provided for in paragraph V below) at which merchandise matters are to, or may, be discussed or considered. If any member of ADC shall be permitted to attend any such meeting, then all members of ADC shall be provided with an opportunity to attend and participate in such meeting and related discussions and matters.

V

It is further ordered, That the officers and directors of ADC, annually, shall appoint the representatives of members of ADC to serve as members of committees or subgroups, including committees and subgroups involved in dealings with manufacturers, distributors or suppliers. Such appointments shall be made on a fair, impartial and non-discriminatory basis, shall be determined on the basis of the trade experience and expressed desires of the respective members of ADC and shall not be determined, directly or indirectly, on the basis of the size or volume of purchases of any member or such member's status as an officer or director of ADC. If any member of ADC has expressed a desire to have its representative serve as a member of a committee or subgroup involved in dealings with manufacturers, distributors or suppliers and has been denied such membership for a particular year, such member shall have the right to have a representative attend, in a non-voting capacity, all meetings and activities of such committee or subgroup, and shall be entitled to receive timely notices thereof to the extent possible in the normal course of business. All notices of meetings and activities shall be communicated on an equal basis to all members of ADC which are entitled to have a representative attend such meetings or activities.

VI

It is further ordered, That respondent ADC notify the Commission at least thirty (30) days prior to any proposed corporate change, such as dissolution, assignment, sale, or reorganization resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change which may affect compliance obligations arising out of this order.

VII

It is further ordered, That at the next meeting of the Board of Directors of respondent ADC, which shall in no event be later than thirty (30) days from the date of service of this order, said Board of Directors shall cause the by-laws of ADC to be amended to include each of the paragraphs of this order and shall terminate and cancel any rule, article, resolution, regulation or by-law of ADC which is contrary to or inconsistent with any provision of this order.

VIII

It is further ordered, That the respondents herein shall within xty (60) days after service upon them of this order, file with the ommission a report, in writing, setting forth in detail the manner d form in which they have complied with this order.

IN THE MATTER OF

PROPOSED TRADE REGULATION RULE FOR THE HEARING AID INDUSTRY

Docket 215-44. Interlocutory Order, June 7, 1979

ORDER DENYING MOTION OF THE NATIONAL HEARING AID SOCIETY

The National Hearing Aid Society (NHAS) by motion of May 22, 1979 has moved that *ex parte* communications between the Commission, any individual Commissioner, or any advisor of a Commissioner, and the FTC staff members assigned to the Proposed Trade Regulation Rule for the Hearing Aid Industry proceeding, Public Record No. 215-44, or the Director of the Bureau of Consumer Protection be prohibited in the above-described proceeding. NHAS further moves that any *ex parte* communications which have already occurred since the initiation of this proceeding if written be placed on the rulemaking record subject to judicial review, or if oral, with a summary thereof. For the reasons set forth below, the Commission denies the motion.

The basic premise underlying the motion is the claim of inherent unfairness in the Commission's procedures which restrict the ability of interested outside parties to communicate with the Commission, but permit unfettered staff contact. Thus, NHAS argues, while the Commission's recently amended Rule 1.18(c) permits outside communications at some stages of a rulemaking proceeding, it fails to subject staff contacts to similar restrictions. NHAS argues that the failure to recognize staff's role as adversarial results in inherent unfairness, thereby denying the procedural due process rights of all other parties participating in the proceeding.

The Commission, as you know, recently reconsidered this issue in amending Rule 1.18(c) of its Rules of Practice, and found that no change in its current practice is required with regard to staff communications. In so doing, the Commission specifically rejecte[illegible] proposals that staff members who participated in rulemakin[illegible] proceedings be prohibited from communicating with any individu[illegible] Commissioner or Commissioners' advisors. *See also* 42 F.R. 605[illegible] (Nov. 28, 1977). It was the Commission's belief that the Administr[illegible] tive Procedure Act's (APA) provisions concerning separation [illegible] functions and *ex parte* communications do not apply to Magnus[illegible] Moss rulemaking. The court in *Hercules, Inc.* v. *EPA,* No. 77-1[illegible] (D.C. Cir., Nov. 3, 1978), noted that the APA has long been constr[illegible] as "allowing the agencies staff to assist agency administrator[illegible] interpreting the record." Slip. Op. at 65. The court in that case refused to find that staff communications invalidated the rule and concluded that any change in the existing law should come from the agencies or Congress. Slip. Op. at 68–69.

The Commission's prior rule placed a total ban on outside communications in order to preserve the integrity of the rulemaking process and to avoid the appearance of unfair access to decisionmakers. The Commission, in amending the rule, decided that a less restrictive standard could serve the same ends, while allowing Commissioners access to potentially useful information from outside parties by requiring placement of the contents of such communications on the public or rulemaking record. The requirement that communications be made available to the public ensures that a full and complete record is accessible both to persons participating in the proceeding and to a reviewing court. This approach is consistent with that taken by the Administrative Conference of the United States in its recommendation 77–3, 1 C.F.R. 305.77–3, and has received the endorsement of Professor Davis. *See, Davis, Administrative Law Treatise,* 553–54 (2d. 3d. 1978).

The Commission also notes that Rules 1.18(a) and (b) require that information that the Commission considers relevant to the rule be made part of the rulemaking record and that the rulemaking record be publicly available. These provisions ensure that all information that the Commission relies upon in adopting a rule, including any internally generated information, will be made part of the rulemaking record and, more important, that the Commission will not consider any information not reflected in the final rulemaking record.

NHAS specifically alleges that a staff memorandum detailing the ·elationship between the FTC and the FDA with respect to regulaion of hearing aids constitutes a harmful *ex parte* contact. NHAS lso notes, however, that this jurisdictional issue was fully briefed ›th in the final staff report as well as in the lengthy comments bmitted by NHAS rebutting the argument. NHAS argues that the herent credibility afforded the staff memorandum by the Commisn puts NHAS at an unfair advantage. This argument is unsuptable. The Commission believes that petitioners prove too much; current procedures have afforded interested parties, including AS, more than substantial opportunity to brief the jurisdictional other issues fully and completely on the rulemaking record.

require all staff communications be recorded would impose antial burdens on the Commission. The range of communicawould be significant, from the trivial to the more important, and their length and complexity could also vary. To the extent that such communications are oral, the recordkeeping requirements could be substantial in terms of time and cost, and the needs of the Commission for fast and flexible means of communicating with its staff about a complex proceeding with a voluminous record could be seriously disserved. The Commission believes that its procedures adequately provide for contacts between non-FTC personnel and the Commission and its own staff and the Commission without endangering the procedural rights of other parties in the proceeding. The Commission's Rules of Practice ensure that all relevant information that the Commission relies upon in adopting a rule will be made a part of the rulemaking record; the Commission will not consider any comments or information that is not reflected in the final rulemaking record. The petition is hereby denied.

IN THE MATTER OF

PROPOSED TRADE REGULATION RULE FOR THE HEARING AID INDUSTRY

Docket 215-44. Interlocutory Order, June 7, 1979

ORDER DENYING MOTION OF THE HEARING INDUSTRIES ASSOCIATION

The Hearing Industries Association on May 30, 1979, filed a Motion to Prohibit Ex Parte Communications Between the Commission and the FTC Staff in the above-captioned proceeding. HIA's motion relied upon and incorporated by reference the National Hearing Aid Society's Motion to Prohibit Ex Parte Communications Between the Commission and the FTC Staff filed May 22, 1979. HIA similarly incorporates by reference in support of its motion pp. 534-542 of Volume IV of its "Final Comments" filed on February 19, 1979.

HIA's motion raises no legal or policy arguments different from those set forth in the NHAS motion. The Commission's order denying that motion is attached. For the reasons set forth therein, HIA's motion is hereby denied.

IN THE MATTER OF

HOWARD ENTERPRISES, INC., ET AL.

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATIONS OF THE FAIR CREDIT REPORTING AND FEDERAL TRADE COMMISSION ACTS

Docket 9096. Complaint, Feb. 8, 1977 — Final Order, June 12, 1979

This order, among other things, requires a Nampa, Idaho firm and its corporate president, engaged in compiling, publishing and distributing consumer reports through franchises and otherwise, to cease disseminating such reports without following reasonable procedures to ensure that reported information is accurate and will be used for permissible purposes. They are prohibited from furnishing "Alert Lists" (lists of consumers who have allegedly passed bad checks) to subscribers who do not have a legitimate business need for information regarding all listed consumers, unless such lists are coded to protect consumers' identity until a subscriber's need has been established. A statement advising recipients of statutory requirements and prohibitions must accompany each disseminated consumer report. Additionally, the order requires respondents to obtain from all franchisees and prospective franchisees a written agreement obligating them to comply with the terms of the order.

Appearances

For the Commission: *Dennis D. McFeely* and *Sharon S. Armstrong.*

For the respondents: *L. Kim McDonald, Smith & McDonald,* Nampa, Idaho.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and the Fair Credit Reporting Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Howard Enterprises, Inc., a corporation, and Ralph R. Howard, individually and as an officer of said corporation, hereinafter sometimes referred to as respondents, have violated the provisions of said Acts, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows (all allegations hereinafter made in the present tense shall include the past tense):

PARAGRAPH 1. Howard Enterprises, Inc. is a corporation organized and doing business under and by virtue of the laws of the State of Idaho, with its principal office and place of business located at 11: Third Ave., Nampa, Idaho.

Respondent Ralph R. Howard is president of the corporate respondent. He formulates, directs and controls the policies, acts and practices of the corporate respondent, including the acts and practices hereinafter set forth. He also engages in the acts and practices hereinafter set forth in his individual capacity. His business address is the same as that of the corporate respondent. [2]

PAR. 2. Subsequent to April 25, 1971, in the ordinary course and conduct of their business, respondents have compiled, published and distributed lists containing, among other things, the names of consumers who have issued forged checks, who have issued checks drawn upon nonexistent accounts, or who have issued checks which have been returned by the drawee bank because of insufficient funds or other reasons.

The information contained in the aforesaid lists concerning consumers whose names appear therein, bears on said consumers' credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics and/or mode of living. Some of the information is used, is expected to be used, or is collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility for credit to be used primarily for personal, family, or household purposes, or is used, is expected to be used, or is collected in whole or in part for use relative to other legitimate business needs for information in connection with business transactions involving consumers reported upon. Therefore, each of the aforesaid lists constitutes a series of consumer reports as "consumer report" is defined in Section 603(d) of the Fair Credit Reporting Act.

Respondents are, for a monetary fee, regularly engaged in the practice of assembling such information on consumers for the purpose of furnishing such lists to third parties, and regularly use a means or facility of interstate commerce for the purpose of preparing and/or furnishing said lists. Therefore, respondents are a consumer reporting agency as "consumer reporting agency" is defined in Section 603(f) of the Fair Credit Reporting Act.

PAR. 3. Respondents furnish the aforesaid consumer reports to persons who respondents do not have reasons to believe:

A. have a legitimate business need for the information upon receipt in connection with a business transaction involving each consumer reported upon,

B. intend to use the information upon receipt in connection with credit transaction involving each consumer on whom the information is furnished and involving the extension of credit to each consumer reported upon, or [3]

C. intend to use upon receipt the information contained in each report for any of the other permissible purposes set forth in Section 604(3) of the Fair Credit Reporting Act.

Further, the furnishing of such consumer reports is not in response to a court order and is not in accordance with the written instructions of each consumer to whom the reports relate.

Therefore, respondents have violated, and are violating, Section 604 of the Fair Credit Reporting Act.

PAR. 4. Respondents fail to maintain reasonable procedures to limit the furnishing of consumer reports to the purposes listed under Section 604 of the Fair Credit Reporting Act, including failure to:

1. require prospective users of consumer reports to certify the purposes for which the information in such reports is sought,
2. require prospective users of consumer reports to certify that the information in such reports will be used for no other purposes than those which have been certified, and
3. make reasonable efforts to verify the uses certified by the prospective users of consumer reports prior to furnishing consumer reports to said users.

Therefore, respondents have violated, and are violating, Section 607(a) of the Fair Credit Reporting Act.

PAR. 5. Respondents furnish consumer reports to persons under circumstances in which there are reasonable grounds for believing that such reports will not be used for a purpose listed in Section 604 of the Fair Credit Reporting Act.

Therefore, respondents have violated, and are violating, Section 607(a) of the Fair Credit Reporting Act.

PAR. 6. Respondents fail to follow reasonable procedures to assure maximum possible accuracy of information concerning the individuals about whom respondents' consumer reports relate inasmuch as respondents fail to provide reasonable procedures to assure maximum possible accuracy in the removal from respondents' consumer report lists of the [4] names of individuals who have paid off checks which have been returned by drawee banks.

Therefore, respondents have violated, and are violating, Section 607(b) of the Fair Credit Reporting Act.

PAR. 7. Subsequent to April 25, 1971, respondents have, in the ordinary course and conduct of their business, sold franchises and business opportunities across state lines to others to engage in businesses conducted by the use of the acts and practices described in Paragraphs Two, Three, Four, Five and Six above. Since the sale of such franchises and business opportunities, respondents have sent and received monies, papers, documents and other materials across state lines and have engaged in interstate travel and communication in connection with the continuing operation by the franchisees of their businesses in such manner as described in Paragraphs Two, Three, Four, Five and Six above. Thus, the respondents have provided and continue to provide to others a means, method and instrumentality to engage in violations of the Fair Credit Reporting Act, and respondents are accordingly engaged in acts or practices which are and have been unfair methods of competition or unfair or deceptive acts or practices in or affecting commerce.

PAR. 8. The acts and practices set forth in Paragraph Seven above are in violation of Section 5 of the Federal Trade Commission Act; the acts and practices set forth in Paragraphs Two, Three, Four, Five and Six above are in violation of the Fair Credit Reporting Act and pursuant to Section 621(a) thereof such acts and practices constitute unfair or deceptive acts or practices in commerce in violation of Section 5 of the Federal Trade Commission Act.

INITIAL DECISION BY LEWIS F. PARKER, ADMINISTRATIVE LAW JUDGE

JANUARY 26, 1978

I. PRELIMINARY STATEMENT

A. History of the Proceeding

This proceeding began on February 7, 1977 with the issuance of a complaint charging that respondents Howard Enterprises, Inc. and Ralph R. Howard had violated the Fair Credit Reporting Act and the Federal Trade Commission Act. Respondents Howard Enterprises and Ralph R. Howard filed their answers to the complaint on May 31, 1977, denying the charges in the complaint. As an affirmative defense, they [2] claimed that they were not engaged in credit reporting and that the Fair Credit Reporting Act therefore did not apply to their activities. They also claimed that they engaged in no unfair or deceptive acts or practices in violation of the FTC Act. Finally, respondents stated that the federal laws referred to in the complaint were unconstitutional as applied to them.

A telephone conference call between myself and counsel for the parties was held on June 2, 1977, and deadlines were set for the filing of lists of witnesses and documents and for evidentiary hearings.

Hearings were held on October 3 and 4, 1977 in Seattle, Washington. Complaint counsel called 11 witnesses. Respondent Ralph R.

Howard was the only witness for the defense. The record was closed on October 31, 1977. Complaint counsel filed their proposed findings of fact and conclusions of law on November 25, 1977. Respondents filed theirs on December 5, 1977.

B. The Allegations of the Complaint

The complaint charges that Howard Enterprises and its president, Ralph E. Howard, have, in the conduct of their business, compiled, published and distributed lists containing, among other things, the names of consumers who have issued forged checks, who have issued checks drawn upon nonexistent accounts, or who have issued checks which have been returned by the drawee bank because of insufficient funds or other reasons.

The complaint states that the information contained in these lists bears on consumers' credit worthiness, reputation, personal characteristics, etc., and that the information is used in whole or in part as a factor in establishing consumers' eligibility for credit or is used in connection with other legitimate business needs for information in connection with business transactions involving consumers reported upon. Therefore, the complaint alleges, respondents' lists are "consumer reports" and respondents are a "consumer reporting agency" as those terms are defined in Sections 603(d) and 603(f) of the Fair Credit Reporting Act (FCRA). [3]

The complaint also alleges that respondents have violated Section 604 of the FCRA by furnishing their reports to persons who they do not have reason to believe (a) have a legitimate business need for the reports, (b) intend to use the reports in connection with a credit transaction involving each consumer on whom the information is furnished, or (c) intend to use the reports for other permissible purposes set forth in Section 604(3) of the FCRA.

According to the complaint, respondents have also violated Section 604(a) of the FCRA by failing to maintain reasonable procedures to limit the furnishing of consumer reports for the purposes listed under Section 604 and by furnishing consumer reports to persons under circumstances in which there are reasonable grounds for believing that such reports will not be used for a purpose listed in Section 604.

The complaint also alleges that respondents have violated Section 607(b) of the FCRA because they do not follow reasonable procedures to assure the accuracy of the information in their reports.

Finally, the complaint alleges that respondents have sold franchises and that they have provided to their franchisees a means, method and instrumentality to engage in violations of the Federal Trade Commission Act.

The following findings of fact, conclusions of law and order are based upon the transcript of testimony, the exhibits received in evidence and the proposed findings filed by complaint counsel and respondents. Proposed findings not adopted herein verbatim or in substance are rejected as not supported by the evidence or as irrelevant.[1] [4]

II. Findings of Fact

A. Description of the Corporate and Individual Respondents

1. Respondent Howard Enterprises is a corporation organized and doing business under and by virtue of the laws of the State of Idaho (CX 1). Its principal office and place of business is located at 111 Third Ave., Nampa, Idaho (Ans. Par. 2). It is a closely held corporation whose officers and directors are Ralph R. Howard, his brother and his wife. Together Ralph R. Howard and his brother Karrell Howard own all the stock in Howard Enterprises (Tr. 147).

2. Respondent Ralph R. Howard has been president and a director of Howard Enterprises since its incorporation and has owned the majority of stock in the corporation at all times (Tr. 147–48). Mr. Howard has formulated, directed and controlled the policies, acts and practices of Howard Enterprises (Ans. Par 2). His business address is 111 Third Ave., Nampa, Idaho (Ans. Par. 2).

B. The Nature of Respondents' Businesses

3. Howard Enterprises is and has been engaged in the business of selling franchises in an "Alert List" system (Tr. 147, 151; CXs 37–46) to purchasers located in Washington and Oregon (CXs 37–41, 42–46). The corporation itself has not engaged in the distribution of Alert Lists (Tr. 148); instead, Mr. Howard operated the Alert List system in southern Idaho and eastern Oregon from December 1974 to June 1977, at which time he sold his distribution rights in those areas to Lynn J. Whitmill, a franchisee (Tr. 148–49, 151, 161; CX 46a–c).

4. The Alert Lists distributed by Mr. Howard were lists of names of individuals who had written checks drawn upon nonexistent

[1] Abbreviations used herein are:

Tr.	: Transcript of the hearings.
CX	: Commission exhibit.
RX	: Respondents' exhibit.
CPF	: Complaint counsel's proposed findings.
Adm.	: Respondents' answers to complaint counsel's requests for admissions (CXs 153A–L and 154A–L).
Ans.	: Respondents' answer.

accounts or who had written checks which had been returned by the drawee bank because of insufficient funds (Adm. 1, 3; Tr. 152). The lists were distributed weekly (CXs 54, 55; Tr. 215). [5]

C. Interstate Commerce

5. Mr. Howard's Alert Lists were disseminated by mail (Adm. 14 and 15) to subscribers in several trade areas in southern Idaho and Oregon (Tr. 151, 157, 161, 168; CXs 29-36).

6. Also, Mr. Howard, on behalf of Howard Enterprises, travelled to the States of Washington and Oregon to assist franchisees in setting up their businesses (Tr. 223, 228-29). Howard Enterprises has sold six franchises which authorize its franchisees to disseminate Alert Lists (CXs 37, 40, 42, 44, 45, 46; Tr. 205-09). These franchisees are authorized to do business in the following areas: (a) southern Idaho, two counties of eastern Oregon, and parts of Wyoming and Utah which fall into the Idaho trade area (CX 46; Tr. 102-03); (b) Oregon State, except for a few eastern Oregon counties, plus three Washington counties (CXs 42, 44; Tr. 225-26); (c) the State of Washington, excluding three counties, and northern Idaho (CXs 37, 40).

7. Sales of all of the franchises were made by respondents from their headquarters in Nampa, Idaho. The franchise territories, with one exception, are located almost entirely outside of Idaho (CXs 37, 40, 42, 44, 45, 46). In some instances, the sales were made to persons then residing outside of Idaho (CX 45; Tr. 227, 229). One franchisee, an Idaho resident, went outside of Idaho to survey the franchise area before investing (Tr. 324). In three instances Mr. Howard travelled from Idaho to other states to assist in getting the franchises started (Tr. 223, 228, 229). Executed franchise agreements were taken or sent outside of the State of Idaho (Tr. 225, 227, 347) and respondents engaged in out-of-state telephone conversations in connection with franchise sales (Tr. 226, 228-29).

8. Except for the Idaho franchisee, all the computer discs containing the program necessary to operate the Alert system were taken outside of Idaho by franchisees (Tr. 223, 227, 326-27; Adm. 63(d)). Other materials and forms necessary to begin the operation of Alert franchisees' systems were also taken outside of Idaho for use (Tr. 316, 326-27; Adm. 69). The respondents provided training to operate franchises in areas wholly or partly outside of Idaho (Tr. 135, 223, 228, 229, 325). [6]

9. Respondents have regularly received from their past and present franchisees across state lines (except for Mr. Whitmill, a franchisee of Mr. Howard) (a) payments constituting the full or

partial cost of Alert List franchises (Adm. 68(a)); (b) periodic monthly payments at the rate of $1.25 per subscriber until early 1976, and at the rate of $1.46 per subscriber thereafter (Adm. 68(b); Tr. 293, 332; CXs 37, 40, 42, 44, 45, 46, par. 4); (c) a monthly computer-printed summary of all amounts owed by the franchisee to the respondents (Adm. 68(c)); and (d) copies of the actual Alert Lists disseminated by the franchisees to their subscribers (Adm. 68(d)). Respondents have made interstate telephone calls in connection with the operation of the franchises between 10 and 30 times (Adm. 67(a) and (b); Tr. 231, 329) and have crossed state lines in connection with the operation of the franchises between 10 and 20 times (Adm. 66(a) and (b); Tr. 231, 318–19, 329).

10. The franchise agreements all provide that respondents shall give advice and instructions to the franchisees, most of whom are located outside Idaho (CXs 37, 40, 42, 44–46, par. 5; Tr. 210–11). In the case of at least one franchisee, this took the form of many written interstate communications from respondents offering names of subscriber prospects, potential new employees, potential groups to contact, and other advice and information (CXs 116, 129–31, 133, 135–37, 139–42, 144, 146, 148–51; Tr. 236–46). It also included assisting a franchisee in soliciting customers outside of Idaho (Tr. 130 A) and helping to collect money owed from subscribers located outside of Idaho (Tr. 130–31).

D. Sources of Information on Alert Lists

11. The information on the Alert Lists which Mr. Howard published was obtained by him from subscribers who mailed Mr. Howard report cards (pre-addressed to Mr. Howard) listing the names of consumers whose checks had been dishonored (Tr. 153). Prior to the summer of 1975, the report card required reporting only of the consumer's name (CX 51; Tr. 213). Later, the report card contained space for bank account numbers or driver's license numbers (CX 50; Tr. 213).

12. The information on the report card was the only information about the check writer Mr. Howard received (Tr. 214). [7]

E. Recipients of Alert Lists

13. There were approximately 180 subscribers in the trade areas in which Mr. Howard disseminated his Alert Lists (CXs 29–36; Tr. 151). For the most part, Mr. Howard's subscribers were retail businesses taking in a high volume of checks, such as grocery stores, clothing stores, pizza parlors, restaurants, and bars (Tr. 157). Checks

were taken by subscribers to pay for the purchase of merchandise, in exchange for cash, and to make payment on open accounts (Tr. 162). A collection agency also received copies of the Alert Lists (Tr. 157).

14. Mr. Howard also disseminated Alert Lists weekly to law enforcement agencies in Idaho and Oregon (Adm. 16, 18; Tr. 157). Lists received by law enforcement agencies were in all respects the same as lists received by subscribers, except that the law enforcement agencies received lists for several trade areas (Tr. 157, 386).

15. Mr. Howard charged a fee to all third parties other than law enforcement agencies to whom Alert Lists were disseminated (Adm. 21). The fee was $15 per month. Later, it was raised to $17.50 per month (Tr. 157–58). For this fee a subscriber was entitled to as many as nine copies of the list (Tr. 158).

F. The Format of the Alert Lists

16. The lists compiled by Mr. Howard bore the designation "Alert Lists" at the top, a date at the left and a geographic area at the right. The names on the lists were organized alphabetically by last name and first name or initial and arranged in columns. Between 30 and 500 names appeared on the lists, depending on the geographic area and date of the list. At the left of each name was an asterisk which designated whether the name had been added in the previous week or a number which indicated how many checks had been reported for that particular individual. At the bottom of each list appeared the post office mailing address used by Mr. Howard and a caution that the list not be reproduced (CXs 2–11, 70–78). Lists compiled and disseminated prior to the summer of 1975 did not identify the consumer except by name (CXs 2–11). [8]

17. The Alert List of July 11, 1975 for the geographic area Ore-Ida (CX 6) is typical in style and format to all Alert Lists compiled and distributed by Mr. Howard until the summer of 1975 (Tr. 172–73), after which time a bank account or social security number was added beneath each individual's name (Tr. 158–59; CXs 70–78).

G. Recipients' Use of Alert Lists

(1) Subscribers

18. The purpose for which Mr. Howard compiled and disseminated Alert Lists for subscribers was to assist them in deciding whether checks proffered to them had the likelihood of becoming dishonored (Tr. 156). It was Mr. Howard's intent that if an individual whose name appeared on the Alert Lists attempted to write a check or cash a check in the subscriber's store, the subscriber would be able to

make an informed judgment to accept or refuse the individual's check (Tr. 186; CXs 54a-b, 55) and the lists were used by subscribers for that purpose (Tr. 186, 372-73, 400-01, 410, 416; CXs 54a-b, 55).

19. The acceptance of a check is part of a business transaction between the merchant and the check writer (Tr. 165). The merchant has a legitimate need for information about the check writing habits of his customers because the information enables the merchant to avoid taking checks which are likely to be dishonored.

20. However, at the time each subscriber received a list, he did not have a use for all of the names on the Alert List (Tr. 400). Mr. Howard testified that, based on his contact with subscribers, it was likely that the subscribers dealt with between 5 percent and 85 percent of the individuals listed on an Alert List (Tr. 192). Testimony of actual users of the lists indicates lower figures. The manager of a clothing store testified that his business attracted 250 to 300 customers per day, had annual sales of $500,000, and took 85 percent of its business in payments by checks (Tr. 405), yet during the 18 months in which his store had subscribed to the Alert Lists, only three persons whose names appeared on the lists had come into the store (Tr. 411). The manager [9] of an auto salvage business which had sales of $40,000 per month (Tr. 413), 50 to 60 percent of whose customers paid by check (Tr. 414), had never in three years had an individual on the list attempt to write a check in the store (Tr. 417). The manager of a farm supply store which did approximately $800,000 worth of business a year during the three years his store had subscribed to the Alert Lists had seen only one individual on the lists in his store (Tr. 397, 401).

(2) Collection Agency

21. Emma Hatfield, the manager of a collection agency which subscribed to the Alert Lists, testified that she uses the lists to see if customers from which she is attempting to collect bills are still on the lists. She does not, however, use the lists directly for the purpose of collecting bills (Tr. 393) and therefore does not use the lists in connection with a business transaction with consumers, for collection of accounts.

(3) Law Enforcement Agencies

22. Mr. Howard also disseminated Alert Lists to law enforcement officials such as local police, state attorneys general, U.S. postmasters, and the U.S. Secret Service (CX 33). He disseminated Alert Lists to these agencies although not ordered to do so by a court (Adm.

26), and without receiving written instructions to provide the lists from consumers whose names appear on the lists (Adm. 27).

23. Law enforcement officials called Mr. Howard to ask for the names of subscribers holding outstanding checks. He was able to provide this information by consulting the master list (Tr. 202-03). William Alfson, a U.S. postal inspector, testified that he scanned the Alert Lists for familiar names in connection with thefts from the U.S. mail resulting in forgeries. He did not undertake investigations as a result of consulting the lists, nor did he obtain convictions as a result of using them (Tr. 382). A detective of the Ada County Sheriff's Office received Alert Lists in connection with his theft detail (Tr. 385). He did not specifically request the lists, nor had he obtained a court order for the lists, does not use them in connection with the granting of credit, the underwriting of insurance, the employment of applicants, the providing of government licenses or benefits, or in connection with a business transaction with the consumers whose names appeared on the lists (Tr. 386-87). **[10]**

H. Certification and Verification by Recipients of Alert Lists

24. Mr. Howard did not obtain from law enforcement agencies which receive Alert Lists any certification that the lists would be used only for the permissible purposes stated in the FCRA nor did he verify the law enforcement agencies' uses of the lists (Tr. 250, 388). Subscribers were not required to certify that they would use the lists only for the purposes listed in the FCRA before receiving the Alert Lists, nor did Mr. Howard verify that the lists were being used only for such purposes (Tr. 160, 250).

25. User witnesses who had made arrangments for their stores to subscribe to the Alert Lists testified that Mr. Howard or his representatives did not at any time ask the subscriber what he or she intended to do with the lists, nor were any restrictions on the use of the lists discussed (Tr. 369, 394, 398, 407).

26. Mr. Howard did not require that subscribers state in writing what uses would be made of the lists or state in writing any agreement as to restrictions on their uses of the lists (Adm. 40(a), (c)). The only writing between the subscriber and Mr. Howard was the order blank (CX 53; Tr. 215), which is silent both as to the subscriber's uses of Alert Lists and as to any restrictions on the subscriber's uses of the Alert Lists.

I. Mr. Howard's Procedures To Assure Accuracy of the Alert Lists

27. Prior to placing a consumer's name on an Alert List, Mr.

Howard did not request the subscriber to send the dishonored check to him (Adm. 43), and he had no way of knowing whether all the names submitted by subscribers were individuals whose checks had in fact been dishonored (Tr. 263).

28. An individual's name appeared on successive Alert Lists until a subscriber notified Mr. Howard that the name should be deleted. Mr. Howard had no regular policy of deleting names from the Alert Lists after 90 days (Tr. 253–54), and some names remained on the lists for as long as 11 months (CX 116). [11]

29. There were two mechanisms for deleting names from the Alert Lists (Adm. 50). Subscribers could mail postcards (CXs 50, 51) to Mr. Howard requesting that a name be deleted (Adm. 45), or subscribers could indicate on an audit sheet that names which they had submitted should be deleted (Adm. 46). The audit (CX 57) consisted of a computer printout of the names of consumers the subscriber had reported with instructions that the names be deleted from the list if the check had been picked up or if the subscriber considered the check uncollectable (CX 57). The audits were mailed out quarterly (Tr. 217). The purpose of the audit was to have subscribers delete names which should no longer appear on the lists (Tr. 218). The fact that subscribers returned the audit sheets indicated that they had failed to use the postcard notification mechanism (Tr. 218–19). The audit system was necessary because the postcard system was inadequate (Tr. 219).

30. Although Mr. Howard requested his subscribers to delete names promptly (Tr. 370), he did not require that subscribers agree in writing to send in delete cards (Tr. 255), he did not impose any penalty on subscribers for failing to submit delete cards on a timely basis (Tr. 256), and he had no way of knowing if a subscriber was sending in his delete cards when he should (Tr. 257). It was also Mr. Howard's policy not to delete a name if a delete card was unsigned (CX 59; Tr. 220). Thus, unless he could recognize the handwriting of the subscriber submitting the delete card, the name could not be deleted even though the individual had already paid the check (Tr. 220).

31. Mr. Howard did not penalize his subscribers for failing to return an audit list (Tr. 256), and he had no way of knowing whether each subscriber returned the audit sheet on a timely basis (Tr. 257) because he made no attempt to keep track of which audit sheets were received. In fact, the only mechanism for uncovering errors in the system was when consumers called him to complain that their names had erroneously appeared on an Alert List (Tr. 203). In those instances, his procedure was to contact the subscriber (Tr. 256), and

he discovered in some of those instances that the subscriber had in fact forgotten to have the consumer's name deleted (Tr. 425). [12]

32. For example, detective Barnes testified that his daughter's name appeared on the Alert List in December 1976. He personally accompanied his daughter to the subscriber's place of business and paid the check. Nevertheless, his daughter's name continued to appear on the Alert Lists until March 1977. When he contacted Mr. Howard, asking that his daughter's name be deleted, he was told it was up to the subscriber to turn in a delete card (Tr. 389).

J. The Businesses Operated by the Franchisees

(1) General Description

33. The manner in which the franchisees operate their Alert List systems is essentially identical to the way Mr. Howard operated his in southern Idaho before it was sold (Tr. 133, 134, 169). Subscribers to the list send in the names of persons who have written checks which have been dishonored (Tr. 115, 306, 327; Adm. 70). These names are compiled by the franchisees into lists by geographic area and the lists are disseminated to the subscribers weekly (Tr. 101, 304, 328; Adm. 71; CXs 12–28, 54–55). The franchisees charged a fee of $15 per month for this service until early 1976, and charged $17.50 per month thereafter (Adm. 78; Tr. 157, 158, 331). Lists are provided free to law enforcement agencies (Tr. 113, 302, 382). Alert Lists containing 3,086 names were distributed by franchisees on July 1, 1977 (CXs 12–28a–b). This is a typical number of names currently circulated on Alert Lists (Tr. 231–32).

34. Names are taken off the lists by subscribers sending in delete cards indicating individuals who have paid outstanding checks (Tr. 119, 213, 307, 349), and except for the present eastern Washington franchise, by the return of audit lists with names marked out (Adm. 69(k); Tr. 218, 349). The current eastern Washington franchisee removes names after they have been on the list for 90 days (Tr. 308). The audit lists are mailed to each subscriber quarterly or every six weeks and contain all the names on the list which have been submitted by that subscriber. The subscriber is instructed, among other things, to delete the names of those who have paid off their checks (Tr. 121, 217–18, 348–49; CXs 57, 86, 129–30). [13]

35. The lists are used by subscribers in determining whether or not to accept checks from persons whose names appear on the lists (Tr. 105, 127, 307, 374, 410). Lists are also sent by franchisees to law enforcement agencies which review the lists for names of persons who are under investigation and for similar law enforcement

purposes (Tr. 112, 202-03, 301-02, 382, 387). The lists distributed to law enforcement agencies are identical to the lists distributed to regular subscribers and include more information than required for identification only (Tr. 113-14, 301).

36. Neither the subscribers nor the law enforcement agencies use all the names on each list at the time received or at any time thereafter (Tr. 124, 310, 353). The subscribers cannot use any of the names on the lists at the time lists are received unless at that moment someone is attempting to write a check (Tr. 191, 400). From 5 to 85 percent of the names on each Alert List are actually used, depending upon the type of outlet and other variables (Tr. 192). Testimony of recipients of Alert Lists indicated that they had actual use for none of the names, or only one to three of the names from all the lists ever received (Tr. 373, 401, 417).

(2) Certification and Verification of Purposes by Franchisees' Subscribers

37. The franchisees do not require subscribers, prior to receiving Alert Lists, to state orally or in writing the purposes for which the information on the Alert Lists will be used (Adm. 81(a); CX 53; Tr. 110, 248-50, 299, 350), nor do the franchisees require, before sending Alert Lists to subscribers, that the subscribers state orally or in writing that the information on the lists will be used for no other purposes than those listed in Section 604 of the FCRA (Adm. 81(c), 81(d); Tr. 110, 124, 248-50, 299, 350). In no instances have franchisees obtained, in connection with lists provided to subscribers and law enforcement agencies, either a court order requiring that such lists or names be provided or written permission from the consumers to do so (Adm. 80(a), (b)). Since the franchisee's subscribers have not certified any purposes in connection with using the lists, the franchisees have not sought to verify any certified purposes (Tr. 250). [14]

(3) Franchisees' Procedures To Assure Accuracy of the Alert Lists

38. The franchisees' procedures to assure accuracy of the Alert Lists were the same as respondent Howard's (Tr. 169) with the exceptions that the present eastern Washington franchisee removes names after 90 days (Tr. 308) and that a former Washington franchisee sent his subscribers audit lists every six weeks instead of every three months (Tr. 349).

39. Franchisees have not obtained written agreements from subscribers providing that only the names of persons who had

written dishonored checks would be put on the Alert Lists (CX 53, 92a-b; Tr. 110, 215, 299, 351) and have failed to verify that bad checks were held for those whose names were sent in (Tr. 117, 214, 306).

40. Franchisees have not obtained the written agreement of subscribers to delete names when checks are paid off (CXs 53, 92a-b; Tr. 110, 215, 299, 350). Sometimes delete cards are not sent in due to poor bookkeeping on the part of the subscriber (Tr. 349) The franchisees have no way of knowing whether subscribers are sending in delete cards when they should (Tr. 120, 308). There are no penalties for failure to return delete cards (Tr. 132, 352). The franchisees were aware that Mr. Howard had reminded his subscribers to send in delete cards and should have known that their subscribers might also be ignoring or forgetting this procedure (Adm. 69(j)).

41. The return of audit lists with names marked out indicates that names could have been removed from the lists earlier (Tr. 121, 218, 349). There is no written agreement with the franchisees' subscribers that audit lists will be returned when appropriate (Tr. 110, 215, 299, 351-52). At least one subscriber simply threw the audit list away (Tr. 419). There are no procedures to help ensure return of the audit lists when appropriate (Tr. 122-23), such as the levying of penalties (Tr. 352).

K. The Purpose of the Alert Lists and Their Use by Recipients for Purposes Other Than Identifying Writers of Bad Checks

42. The purpose of the Alert Lists is to give merchants a means to identify consumers who may have written bad checks [15] (Tr. 106, 156). There is no evidence that the Alert Lists were designed to provide information about a consumer's credit worthiness, credit standing or credit capacity, or, aside from what might be inferred about the character of the writer of bad checks, any specific information about a consumer's character, general reputation, personal characteristics, or mode of living.

43. The Alert Lists were used by recipients only to identify consumers who may have written bad checks. They were not used for purposes of granting credit (Tr. 124, 315, 421) or insurance (Tr. 187, 380) or for employment purposes (Tr. 187).

44. The use by the recipients of the Alert Lists in the circumstances described above indicates that they were not used solely for purposes authorized by Section 604 of the FCRA.

45. The writing of bad checks, in the opinion of some merchants, reveals the writer's bad character (Tr. 375-76, 395, 402, 410). To some extent then, it can be said that the Alert Lists, although not

disseminated for that purpose, do relate to a consumer's character, general reputation or personal characteristics.

III. Conclusions of Law

Jurisdiction

The Commission's jurisdiction over respondents' business activities depends on whether Howard Enterprises is a "consumer reporting agency" as defined in Section 603 (f) of the FCRA:

> The term "consumer reporting agency" means any person which, for monetary fees, dues, or on a cooperative nonprofit basis, regularly engages in whole or in part in the practice of assembling or evaluating consumer credit information or other information on consumers for the purpose of furnishing consumer reports to third parties, and which uses any means or facility of interstate commerce for the purpose of preparing or furnishing consumer reports.

[16] "Consumer reports" are defined in Section 603(d) of the FCRA:

> The term "consumer report" means any written, oral, or other communication of any information by a consumer reporting agency bearing on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living which is used or expected to be used or collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility for (1) credit or insurance to be used primarily for personal, family, or household purposes, or (2) employment purposes, or (3) other purposes authorized under section 604. . . .

According to complaint counsel, respondents' bad check lists are a series of "consumer reports" and respondents' dissemination of those lists makes Howard Enterprises a "consumer reporting agency." Although complaint counsel can muster in support of their position a court of appeals decision, several consent agreements and informal advisory opinions by the Commission's staff, I do not share complaint counsel's view, for the decision of the Ninth Circuit, the consent greements and the advisory opinions are based on a literal reading f the FCRA which I cannot accept. In addition, they ignore ongressional history which tends to support respondents' claim that e Commission has no jurisdiction over their activities.

The key question in this case is whether respondents provide onsumer reports" to their customers. If I were to follow the Ninth rcuit's decision in *Greenway* v. *Information Dynamics, Ltd.*, 524 d 1145 (9th Cir. 1975), the answer would have to be yes, for there court of appeals affirmed a district court decision which held t a bad check reporting service almost identical to respondents' a consumer reporting agency (399 F.Supp. 1092 (D. Ariz. 1974)).

Section 603(d)(1) and (2) of the FCRA defines consumer reports in terms of the main purposes for which they are disseminated: [17]

> . . .for the purpose of serving as a factor in establishing the consumer's eligibility for (1) credit or insurance to be used primarily for personal, family or household purposes, or (2) employment purposes. . . .

The lower court, believing that bad check lists were not used to establish a consumer's eligibility for credit, insurance or employment, turned to another Section (603(d) (3)) to justify FCRA jurisdiction over Information Dynamics, Ltd., holding that bad check lists had a bearing on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living and were used for "other purposes authorized under Section 1681(b)(3)(E)" (Section 604(3)(E)). Section 604(3)(E) authorizes disclosure of consumer information to a person whom the disseminator has reason to believe:

> otherwise has a legitimate business need for the information in connection with a business transaction involving the consumer.

The court of appeals adopted the lower court's decision but apparently to bolster its conclusion, held, in defiance of accepted understanding,[2] that "a check itself is, essentially, an instrument of credit." 524 F.2d at 1146. In a rather convincing dissent, Judge Wright argued that Section 604(3)(E) should not be used to establish jurisdiction over a business which provides information unrelated to credit, insurance or employment.

Judge Wright recognized that which the court of appeals and complaint counsel ignore: The main thrust of Section 604 is to limit the permissible purposes for which a consumer reporting agency may furnish a consumer report rather than to confer jurisdiction over businesses whose activities have little to do with those which Congress decided to regulate.

The evidence developed in this case reveals that while information that a person has passed a bad check bears to [18] some extent on his character or general reputation, the information was not used or collected for the purpose of serving as a factor in establishing the consumer's eligibility for credit or insurance or for employment purposes (Section 603(d)(1)-(2)). The only section of the FCRA which might arguably confer jurisdiction over respondents is Section 603(d)(3), and it is this, with its incorporation of Section 604(3)(E),

[2] See § 3-104, *Uniform Commercial Code; Greenway, supra*, at 1146 (Dissenting opinion of Judge Wright).

upon which complaint counsel rely, just as did the court in *Greenway*.

I concede that businesses which subscribe to respondents' service have a legitimate need for the information provided and if I were to limit my inquiry to the literal wording of Section 604(3)(E), I would have to conclude that Howard Enterprises is providing consumer reports. But any business which seeks information of whatever kind has a "legitimate need" for it. Read in the way complaint counsel would have it, Section 604(3)(E) would expand the definition of consumer report to an unlimited extent. Indeed, the definitions in Section 603(d)(1) and (2) would become superfluous.

I agree with complaint counsel that Congress did intend to expand the definition of consumer report beyond that spelled out in Section 603(d)(1) and (2). See *Judicial Construction Of The Fair Credit Reporting Act: Scope And Civil Liability,* 76 Colum. L. Rev. 458, 471 and n. 84 (hereafter "Judicial Construction"). However, I believe that Congress intended the courts and the Commission to apply the language of Section 604(3)(E) with some discretion, utilizing it only where the expansion of jurisdiction is compatible with the FCRA.[3]

[19] Complaint counsel argue, instead, for a literal reading of Section 604(3)(E). I cannot accept this approach. Going beyond the literal language of the statute, and turning to the congressional history of the FCRA, I find that it supports respondents' claim that the Commission does not have jurisdiction over their activities. A conference report (116 Cong. Rec. 35847-35851 (October 8, 1970)) issued after the FCRA bill was added by the Senate to H.R. 15073, 116 Cong. Rec. 32639 (1970), stated:

> Your conferees also intend that the definition of "consumer credit report" not include protective bulletins issued by local hotel and motel associations, and circulated only to their members, dealing solely with transactions between members of the associations and persons named in the report. 116 Cong. Rec. at 35850.

Complaint counsel discount this statement, claiming first that bad check lists such as those circulated by respondents are not "protective bulletins." Second, they argue that discussions of the conference report by Senators Proxmire and Bennett and Representative Widnall so confuse the issue that one cannot tell with any assurance what congressional intent is. It is true that Senator Proxmire "clarified" the quoted statement in the conference report by stating

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[3] See "Judicial Construction" at 471:

> Even where there is no direct conflict [between Sections 603(d)(1)-(2) and 604(3)(E)], it must be remembered that Section [604's] primary function is to delineate the purposes for which consumer reports may be furnished. When utilized as a definitional provision in conjunction with Section [603(d)], a less than literal reading of its terms may be required to effectuate the legislative intent with respect to coverage of the Act.

that "[t]o the extent that a local hotel or motel association compiles credit or other information . . .it is making consumer reports as defined under Section 603(d) . . . ." (116 Cong. Rec. 35941 (Oct. 9, 1970)). However, Senator Bennett said: "To restrict an association from providing information to its own members or individuals who have not paid their motel or hotel bill or who have paid such bills with a check which is dishonored seems to be absurd." 116 Cong. Rec. 35942 (Oct. 9, 1970). During debate on the conference report, Representative Widnall summed up the views of the two senators and concluded with some frustration:

> How does anyone interpret congressional intent with this kind of a record? I do not believe there are many of us here in the House who would deliberately vote to restrict the dissemination of the names of known criminals yet as a result of bypassing our prescribed legislative procedures we are not certain what we are voting for in title VI of this bill. 116 Cong. Rec. 36574 (Oct. 13, 1970).

[20] Although "protective bulletins" which identify known criminals or individuals who are being sought by law enforcement agencies can be viewed as "consumer reports" under a literal reading of Section 604(3)(E), the Commission has recognized, in an interpretation under the FCRA, the intent of Congress to exclude at least some protective bulletins from the definition of "consumer report." See 16 CFR 600.2. Despite the obvious harm to those who might be listed incorrectly as criminals or fugitives, the Commission held in this interpretation that protective bulletins of the kind described above were not "consumer reports" because the information was not collected for consumer reporting purposes and because it cannot reasonably be anticipated that it will be used in connection with a legitimate business transaction with the persons reported upon.

Complaint counsel argue that in contrast to protective bulletins, bad check lists are provided for a legitimate business need[4] and that, for that reason, these lists are subject to FCRA requirements. The answer to this argument is that the conference report discussed and intended to exclude from FCRA coverage, the dissemination of

[4] Complaint counsel are somewhat inconsistent in their use of the "legitimate business need" language of Section 604(3)(E) for they claim that the Commission has jurisdiction over bad check list services because the recipients have a legitimate business need for them, yet also argue that respondents have violated Section 604 because the recipient could *not* have a legitimate business need for all of the names on the lists (CPF Brief, pp. 14–15). I agree with complaint counsel that this is not a fatal inconsistency, but it does suggest that something more than a literal reading of Section 604(3)(E) is needed in this case.

protective bulletins (listing those who skipped without paying their bills or who passed bad checks)[5] which [21] obviously were designed to be used in connection with legitimate business transactions between hotels and their customers. The protective bulletins referred to in the conference report were not limited to lists of names of known criminals, and I do not accept complaint counsel's arguments that Representative Widnall's reference to "known criminals" during debate calls for limiting the language of the conference report to protective bulletins listing only "known criminals."[6]

In conclusion, I find that Congress intended to exclude from FCRA jurisdiction the dissemination of information about persons who pay for their hotel bills with bad checks even though such dissemination is (a) for "other purposes authorized under section 604" (Section 603(d)(3)) and (b) even though the recipient "has a legitimate business need for the information in connection with a business transaction involving the consumer." (Section 604(3)(E)). I see no reason why respondents' business, which disseminates the same kind of information, should be treated differently.

Furthermore, the history of the FCRA reveals that what prompted congressional action was not the unregulated dissemination of information about passers of bad checks. Complaint counsel recognize this:

> There is no dispute that the bulk of the testimony before Congress when it formulated the FCRA concerned abuses by giant credit bureaus maintaining files on millions of consumers. Nor can it be disputed that most of the abuses testified to concerned consumers' credit, employment and insurance transactions (CPF Brief, p. 7).

A description of the typical credit or insurance report reveals how far removed it is from the very simple information provided by respondents: [22]

> The credit report typically contains information on the consumer's present and past employers, income, current indebtedness, and general financial history, including such items as past performance on credit accounts and loans, bankruptcies, suits or judgments against the subject, and tax or other liens against his property. This information is gathered from the subject's credit application, investigation of the credit sources listed, and the public record. Underwriters of insurance, as well as employers and landlords, frequently demand an even more thorough investigation of

[5] Representative Widnall stated:

> This language was included because evidence submitted to members of the Consumer Affairs Subcommittee disclosed that hotels and motels are plagued by people who skip without paying bills–or pay with checks that bounce. 116 Cong. Rec. 36574 (Oct. 13, 1970).

[6] I take it that Representative Widnall's reference to "known criminals" was a deliberate exaggeration designed to bolster his arguments that services providing lists of persons who passed bad checks need not be subject to the requirements of the FCRA because those who pass bad checks are, in his words, "obviously dishonest." 116 Cong. Rec. 36574 (Oct. 13, 1970).

the subject. To meet these needs, a second type of consumer reporting agency has developed and, like their sister credit bureaus, these preparers of "investigative consumer reports" are thriving. Investigative reports are more concerned with the subject's character, reputation and mode of living, and may contain information on any aspect of one's personal life, ranging from housekeeping proficiency and yard care, to associates' reputation, to drinking and sexual habits. Judicial Construction at 459–60.

Of course, one must give some meaning to the "other purposes" language in Section 603(d)(3). But as I read that section, it confers jurisdiction over activities which although not explicitly referred to in Section 603(d)(1)–(2), have some connection with the underlying purpose of the FCRA. I do not believe that the dissemination of bad check lists meets this requirement. This fact, coupled with the conference report's reference to exclusion of bad check list services from coverage under the FCRA leads to the conclusion that the Commission does not have jurisdiction over respondents' activities.

ORDER

Therefore,

It is ordered, That the complaint be, and it hereby is, dismissed.

OPINION OF THE COMMISSION

BY PERTSCHUK, *Commissioner:*

I. BACKGROUND

On February 7, 1977, the Commission issued a complaint charging that respondents, Howard Enterprises, Inc. and Ralph R. Howard, violated the Fair Credit Reporting Act ("FCRA"), 15 U.S.C. 1681, *et seq.* and Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45, in connection with the distribution of lists of the names of individuals who have allegedly passed bad checks ("Alert Lists"). The central question presented by this proceeding is whether the Alert Lists constitute "consumer reports" under the terms of the FCRA.

Hearings were held on October 3 and 4, 1977, in Seattle, Washington before the administrative law judge (the "ALJ"). The ALJ issued his initial decision on January 26, 1978, in which he concluded that the Alert Lists are not "consumer reports," under the FCRA, and that, therefore, the Commission does not have jurisdiction over respondents' activities. Accordingly, the ALJ issued an order dismissing the complaint. Counsel supporting the complaint filed a notice of appeal of the ALJ's initial decision on February 14, 1978. Based on the mutual consent of the parties, oral argument was omitted by our order of April 7, 1978. [2]

We have reviewed the record and examined the provisions of the FCRA, its legislative history, as well as other law pertaining to the issues raised in this proceeding. Except as indicated below, we concur in and adopt the findings of fact set forth in the ALJ's initial decision. However, for the reasons discussed below, we have concluded that the Alert Lists are "consumer reports" as defined in the FCRA and that the Commission does have jurisdiction over the Respondents' activities.[1]

II. Summmary of Respondents' Practices

Respondents Howard Enterprises, Inc. and Ralph R. Howard, its founder, president, and majority stockholder, are engaged in the Alert List business. The corporation sells Alert List franchises in a five state area in the Pacific Northwest. (IDJ at 3, 5.) Individual respondent Howard personally operated an Alert List system in parts of Idaho and Oregon from December, 1974 until June 1977. (IDJ at 3–4.)

As the ALJ found, Alert Lists are lists of names of individuals whose checks have been dishonored by the drawee bank when presented for payment. (IDJ at 4.) The lists, which were compiled and distributed weekly by Mr. Howard, bore the designation "Alert List" at the top, a date at the left and a geographic area at the right. There were between 30 and 500 names on each list, organized alphabetically by last name. Initially the lists only identified the consumer by name; however, after the summer of 1975, a bank account or social security number was added beneath each name. (IDJ at 16.)

The ALJ also found that Alert List subscribers were generally retail businesses such as grocery stores, department stores and restaurants.[2] These businesses accepted checks in payment for merchandise, in exchange for cash or as partial payment on open accounts. (IDJ at 13.) [3]

Mr. Howard testified that his purpose in compiling Alert Lists was to assist subscribers in deciding whether to accept checks from their customers. (IDJ at 18.) The ALJ agreed, and found no evidence that the lists were *designed* for any broader purpose. (IDJ at 18, 42–45). However, the fact that an individual wrote a bad check could certainly be seen as bearing on credit worthiness, and some evidence in the record indicates that Alert Lists could have been used in

[1] The following abbreviations are used in this opinion: IDJ - Initial Decision of Administrative Law Judge (cited by paragraph except where otherwise indicated); TR - Transcript of Testimony; CX - Commission's Exhibit; CCB - Complaint Counsel's Appeal Brief; RAB - Respondents' Answering Brief; CRB - Complaint Counsel's Reply Brief; Adm - Respondents' Answers to Complaint Counsel's Request for Admissions.

[2] Other recipients included a collection agency and law enforcement agencies. IDJ at 21.

establishing a consumer's eligibility for credit. (*See, e.g.,* Tr. 376-77; Tr. 53; Tr. 314-15.)

According to the ALJ, the information on the Alert Lists was derived from "report" cards which participating merchants sent to Mr. Howard periodically, listing names of consumers whose checks had not been honored. These cards were the only information about the check writers received by Mr. Howard. (IDJ at 11-12.) He did not require that the dishonored check be sent to him, nor did he obtain any other independent verification that the individuals whose names he placed on the list had in fact written dishonored checks. (IDJ at 27.)

The ALJ also found that Mr. Howard had no regular policy of deleting names from Alert Lists after 90 days, and that some names remained on the lists for as long as eleven months. (IDJ at 28.) The only mechanisms for correcting the lists were for subscribers to mail a postcard to Mr. Howard requesting deletion of a name, or to indicate on quarterly computer printouts, termed audit lists, that a name should be deleted. (IDJ at 29.) In other words, an individual's name appeared on successive Alert Lists until a subscriber notified Mr. Howard otherwise in writing. (IDJ at 28.) With only one exception, these procedures were also used by Alert List franchisees. (IDJ at 38.)[3]

Although the accuracy of Alert Lists depended upon corrections submitted by subscribers, this part of the system was not policed. Mr. Howard and other franchisees made the audit lists and delete cards available, but the ALJ found that they did not require that cards or lists be returned on a timely basis. (IDJ at 30-31.) Nor was any attempt made to monitor which audit lists were returned, despite the fact that instances occurred in which subscribers neglected to request that names erroneously appearing on the Alert List be deleted. (IDJ at 31.) [4]

The record also indicates that respondents did not attempt to regulate the manner in which subscribers handled Alert Lists. For example, subscribers were not required to agree to keep the lists confidential. As a result, the lists were posted by some subscribers in places where they were visible to the public (Tr. at 123, 255, 309, 400 408 and 415).[4]

[3] The ALJ noted that one franchisee does remove names after 90 days. (IDJ at 38.)

[4] One consumer complained to Howard that "you are advertising me as a criminal or thief where all the pul can see my name." (CX 62.) This letter was used by Mr. Howard as promotional material. (Adm 69(a); Tr. 350.)

III. ARE ALERT LISTS "CONSUMER REPORTS" AS DEFINED IN THE FCRA?

In his initial decision, the ALJ ruled that Alert Lists are not "consumer reports" as defined in the FCRA. The ALJ recognized that the information on Alert Lists bears on a consumer's character or reputation, that businesses which subscribe to Alert Lists have a legitimate business need for the information, and that a literal reading of the statute compels the conclusion that Alert Lists are consumer reports. (IDJ at p. 18.) Nonetheless, he rejected a literal reading of the statute, stating that the "Congress intended the courts and the Commission to apply the language of Section 604(3)(E) with some discretion, utilizing it only where the expansion of jurisdiction is compatible with the [purpose of] the FCRA." (IDJ at p. 18.) The ALJ also concluded that Alert Lists are essentially the same as "protective bulletins" and that an exemption from the statute for protective bulletins is recognized in the legislative history of the FCRA. (IDJ at p. 21.)

On this, the key issue, we reverse the ALJ's holding. The express terms of the FCRA establish that Alert Lists fall within the definition of "consumer reports." Moreover, any other interpretation, in our opinion, would contravene the purposes of the FCRA and would be inconsistent with its legislative history.

A. THE EXPRESS TERMS OF THE FCRA

In determining whether respondents' activities fall within the scope of the FCRA, it is necessary to construe certain definitional terms of the Act. Section 603(f) defines a "consumer reporting agency" to be any person or institution which "regularly engages in whole or in part in the practice of assembling or evaluating consumer-credit information or other information on consumers for he purpose of furnishing consumer reports to third parties . . . ." 5 U.S.C. 1681a(f).

The definition of a "consumer report" appears in Section 603(d) hich provides, in part: [5]

> e term "consumer report" means any written, oral or other communication of any rmation by a consumer reporting agency bearing on a consumer's credit thiness, credit standing, credit capacity, character, general reputation, personal acteristics, or mode of living which is used or expected to be used or collected in le or in part for the purpose of serving as a factor in establishing the consumer's ility for (1) credit or insurance to be used primarily for personal, family or hold purposes, or (2) employment purposes, or (3) *other purposes authorized Section 604*. . . . (Emphasis added.)

As the emphasized language indicates, the definition of "consumer report" specifically incorporates by reference Section 604. Thus, Section 604 serves two functions, the primary one being to establish the permissible uses of consumer reports, and, the second, to add content to the Section 603(d) definition of a consumer report.

Under one permissible purpose, Section 604(3) authorizes disclosure of consumer reports to a person whom the disseminator has reason to believe:

> (E) Otherwise has a legitimate business need for the information in connection with a business transaction involving the consumer.

When Sections 603(d) and 604(3)(E) are read together, as they must be for definitional purposes, the resulting standard can be stated in clear, if lengthy, terms: when a person or institution disseminates information bearing on any of the seven criteria relating to a consumer, listed in Section 603(d), to a third party, and the person or institution knows or expects such information will [6] be used in connection with a business transaction involving the consumer,[5] then that information is a "consumer report."[6]

The information on respondent's Alert Lists satisfies the elements of this definition.[7] First, the information disseminated in the Alert Lists necessarily bears on at least one, if not all, of the seven consumer characteristics in the definition of a consumer report.[8] Indeed, the ALJ specifically found that Alert Lists bear upon a consumer's character, general reputation and [7] personal characteristics. (IDJ at 45.)[9] Second, Alert Lists are used or expected to be

[5] In the context of its definitional function, we interpret Section 604(3)(E) as including only business transactions between report users and consumers acting as consumers. This narrow interpretation is consistent with the clear Congressional intent that business reports not be classified, *per se*, as consumer reports. S. Rep. No. 517, 91st Cong., 1st Sess. 1 (1969). In light of this interpretation of Section 604(3)(E), we do not share the ALJ's concern that the incorporation of Section 604(3)(E) "expand[s] the definition of consumer report to an unlimited extent." (IDJ at p. 18).

[6] This is the test adopted by the District Court and affirmed by the Court of Appeals in *Greenway* v. *Information Dynamics, Ltd.*, 399 F. Supp 1099 (D. Ariz. 1974), *aff'd* 524 F.2d 1145 (9th Cir. 1975).

[7] Respondents urge us to reject this interpretation of the statute, arguing that the use of the word "eligibility" in Section 603(d) demonstrates that only those purposes listed in Section 604 for which a person could be "eligible" are included in the definition of consumer report, and further that a person could not be eligible to cash a check. (RAB at 4, 5, 7.) It appears, however, that the number "(1)" is misplaced in the codified statute, since one cannot be eligible for "employment purposes" or for "other purposes." The statutory syntax is only consistent and meaningful if the "(1)" is read in between "for" and "the purpose of," thus making the first category

> ". . .for (1) the purpose of serving as a factor in establishing the consumer's eligibility for credit or insurance. . . ."

[8] The characteristics are credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, and mode of living.

[9] Section 603(d) provides that the term " 'consumer report' means any written, oral or other communication *** which is used or *expected to be used* ***." (Emphasis added.) As the court held in *Belshaw* v. *Credit Bureau of Prescott*, 392 F. Supp. 1356, 1359-60 (D. Ariz. 1975):

> ". . . 'consumer report' must be interpreted to mean any report . . . of information that *could be used* for one of the purposes enumerated in [Section 603(d)] . . . ." (Emphasis in the original.)

(Continued)

used in connection with business transactions involving consumers.[10] Again, the ALJ specifically found that the acceptance of a check is part of a business transaction between the merchant and the check writer and that the Alert List information has been used by merchants to avoid taking checks which are likely to be dishonored. (IDJ at 19.)

Judicial decisions support our conclusion that the FCRA applies in this case. For example, the facts in *Greenway* v. *Information Dynamics Ltd.,* 399 F. Supp. 1092 (D. Ariz. 1974) *aff'd* 524 F.2d 1145 (9th Cir. 1975), are virtually identical to the facts in this case. In *Greenway,* the defendant distributed to subscribing merchants the following information concerning consumers who allegedly passed bad checks: their names, drivers' license numbers, checking account numbers, number of checks returned, and, in some cases, the reasons for the return of the checks. There, the Court of Appeals for the Ninth Circuit concluded that such information constitutes a "consumer report," as defined in the FCRA. *See also Belshaw* v. *Credit Bureau of* [8] *Prescott,* 392 F. Supp. 1356 (D. Ariz. 1975); *Beresh* v. *Retail Credit Co.,* 358 F. Supp. 260 (C.D. Cal. 1973).[11]

B. THE PURPOSES AND LEGISLATIVE HISTORY OF THE FCRA

The FCRA serves important public interests by ensuring that consumer reports are prepared and disseminated in a manner that is fair and equitable to consumers. More specifically, the FCRA is intended, *inter alia,* to ensure the accuracy of consumer reports and to protect the individual consumer's right to privacy. Under Section 602(b), the purpose of the FCRA is:

> to require that consumer reporting agencies adopt reasonable procedures for meeting the needs of commerce, for consumer credit, personnel, insurance, and other information in a manner which is fair and equitable to the consumer, with regard to the confidentiality, accuracy, relevancy and proper utilization of such information . . . .

The privacy purpose of the Act is specifically articulated in Section 602(a):

The type of information on Alert Lists and other evidence suggests that Alert Lists could be used as a factor in establishing a consumer's eligibility for credit, thus providing an additional basis for the determination that Alert Lists constitute consumer reports. See p. 3, *supra.*

[10] Alternatively, the second element of the definition can be satisfied by establishing that the Alert Lists are used or expected to be used for any one of the other purposes enumerated in Sections 603(d) and 604.

[11] District court decisions cited in the dissenting opinion in *Greenway* v. *Information Dynamics, Ltd., supra,* at 1147-48, are distinguishable from this case in that they pertain to credit reports in connection with a business entity in which the consumer was a principal, not one involving the consumer in his personal and individual capacity. *See, e.g., Wrigley* v. *Dun & Bradstreet,* 375 F. Supp. 969 (N.D. Ga. 1974), *aff'd* 500 F.2d 1183 (5th Cir. 1974); *Sizemore* v. *Bambi Leasing Corp.,* 360 F. Supp. 252 (N.D. Ga. 1973); *Fernandez* v. *Retail Credit Co.,* 349 F. Supp. 652 (E.D. La. 1972).

There is a need to insure that consumer reporting agencies exercise their grave responsibilities with fairness, impartiality, and a respect for the consumer's right to privacy.

As the evidence in the record indicates, the manner in which Alert List systems are operated has resulted in a significant invasion of the privacy of individual consumers. For example, operators of the Alert List systems do not require subscribers to agree that the lists will not be publicly displayed (Tr. 110, 299, 255, 351; CX 87, 92a-b), and some subscribers post the lists where they are visible to the public (Tr. 123, 255, 309, 400, 408, 415). *See also,* p. 4, *supra.* Additionally, the ALJ's findings of fact establish that the procedures followed by respondents were totally inadequate to ensure the accuracy of the Alert Lists and the fair and equitable treatment of consumers. (*See* IDJ at 27-32 and 38-41.) [9]

The ALJ also concluded that Alert Lists are indistinguishable from "protective bulletins" (IDJ at p. 21) and, accordingly, are exempted from the provisions of the FCRA. "Protective bulletins" are lists of the names (and sometimes photographs) of consumers who have issued worthless checks or who may have criminal records or arrest warrants outstanding. Such lists are circulated by the members of local hotel and motel associations or other such organizations.

As indicated by the discussion in the initial decision and complaint counsel's brief, the legislative history on the protective bulletin issue is far from clear. If anything emerges from that history, it is that Congress intended whatever exemption may have been created to apply only to a narrow category of bulletins. For example, the House managers of the FCRA stated that

Your conferees also intend that the definition of "consumer report" not include protective bulletins issued by local hotel and motel associations, and circulated *only* to their members, dealing *solely* with transactions between members of the associations and persons named in the report. (Emphasis added.) H.R. No. 1587, 91st Cong., 2d Sess. 28 (1970), *reprinted in* [1970] U.S. Code Cong. & Ad. News, 4411, 4414.[12]

A previous interpretation of the protective bulletin exemption by the Commission is consistent with this limited view. In 16 C.F.R. 600.2(b), the Commission stated that the FCRA does not apply to certain communications, described as:

a series of descriptions, usually accompanied by photographs, of individuals who are being sought by law enforcement authorities for alleged violations of criminal laws.

[12] However, the existence of even such a limited exemption is called into question by subsequent statements of Senator Proxmire who was the Act's author and leader of the Senate conferees. *See 116 Cong. Rec. 35941 (Oct. 9, 1970).*

However, the interpretation adds that the exemption is destroyed if such bulletins contain information used for any of the purposes described in Section 603(d).

With the purposes and history of the FCRA in mind,[13] we do not find it difficult to distinguish Alert Lists from protective bulletins. On its face an Alert List contains [10] more detailed personal information about individuals than a protective bulletin does, including such items as social security numbers, bank account numbers, and indications of how long the name has been on the list and how many bad checks reported. (IDJ at 16–17) Additionally, the consumers whose names appear on Alert Lists are not, at least for the most part, "forgers, swindlers or other criminals" for whom arrest warrants are outstanding. *See* 16 C.F.R. 600.2(c). More significantly, Alert Lists are not the result of cooperative activities by local hotel and motel or other trade associations, incidental to the primary commercial purpose of their members, about which some members of Congress expressed concern. Rather, they are the product of a professional reporting company whose express and exclusive functions are to compile consumer credit information and to disseminate it to a broad range of subscribers. We therefore conclude that the information on respondents' Alert Lists constitutes "consumer reports" within the meaning of Section 603(d), and is subject to the statutory restrictions.

IV. Violations of the FCRA and FTC Act

Under Section 603(f) of the FCRA, a "consumer reporting agency" is any person which (1) regularly assembles the specified types of information on consumers for the purpose of distributing it to third parties, (2) for a fee, (3) by means of interstate commerce. The ALJ's findings of fact establish that respondent Howard meets these three requirements. Mr. Howard regularly assembled the information on the Alert Lists for the purpose of distributing it to third parties (IDJ at 3, 4, 11, 13, 14). He engaged in these activities for a fee to each subscriber of $15.00 per month (later raised to $17.50) (IDJ at 15) and utilized means and facilities of interstate commerce in connection therewith. (IDJ at 5, 11, 13, 14.) Therefore, respondent, Ralph R. Howard, was acting as a "consumer reporting agency" as that term is defined in the statute.

As a consumer reporting agency under the FCRA, respondent is subject to the statutory limitations on the manner in which

[13] Representative Widnall, a House conferee, stated that questions about the protective bulletin "exemption" hould be resolved "in light of [the FCRA's] real objectives as set forth in the statement of findings and purpose in ection 602." 116 Cong. Rec. 36574 (Oct. 13, 1970).

information is compiled, maintained and disseminated. The statute requires that consumer reports be furnished to third parties only for the permissible purposes listed in Section 604. It also establishes certain "compliance procedures" in Section 607 which obligate reporting agencies to, among other things, obtain certification from recipients that the information will only be used for permissible purposes and to assure "maximum possible accuracy" when preparing consumer reports. Additionally, only limited information may be provided to governmental agencies unless Sections 604 and 607 are complied with. We now proceed to discuss whether respondents' practices violate these standards of conduct as charged in the complaint. [11]

A. DISSEMINATION OF CONSUMER REPORTS WITHOUT BUSINESS NEED

Alert List subscribers have a legitimate business need for information about a particular individual only in the context of a consumer transaction with that individual, such as when the individual offers a check in payment for a purchase. As noted, however, each Alert List contains the names of from 30 to 500 individuals who have reportedly passed bad checks. Therefore, as the ALJ found, subscribers did not have a legitimate business need for information regarding all of the individuals on the list. (IDJ at 20.) Testimony from Mr. Howard and his subscribers indicates that, in practice, some subscribers may have dealt with 5 percent or fewer of the individuals listed and that none had dealings with all of those individuals, the highest estimate being 85 percent. *Id.*

By providing subscribers with consumer credit information for which they had no legitimate business need, respondent Howard violated Section 604 of the FCRA. The Commission has previously indicated that the permissible purpose for furnishing the consumer report must exist at the time the report is distributed; it is not sufficient that the consumer report be distributed in anticipation that a permissible purpose will subsequently arise. 16 C.F.R. 600.1(c).

We note, as complaint counsel correctly point out in their brief, that these violations would not have occurred if respondent Howard had encoded the Alert Lists. (CCB at 21.) Coding is the use of a unique identifier, other than a name, through which the subscriber may identify the consumer and decode the information in connection with a business transaction. Thus, the decoded information will become available to the subscriber only at that point when a "legitimate business need for the information in connection with a business transaction involving the consumer" arises, as required by Section 604.[14]

B. DISSEMINATION TO LAW ENFORCEMENT AGENCIES

Law enforcement agencies, like other users, are entitled to receive consumer reports for the permissible purposes set forth in Section 604 of the FCRA. In addition, Section 608 provides another permissible purpose: [12]

Notwithstanding the provisions of Section 604, a consumer reporting agency may furnish identifying information respecting any consumer, limited to his name, address, former address, places of employment, or former places of employment, to a governmental agency.

The Alert Lists disseminated to law enforcement agencies contain more information than is allowed under Section 608 in that they report the consumer's alleged issuance of a bad check, the consumer's bank account or social security number, the number of bad checks written and whether the check was reported during the preceding week. In addition, the ALJ's findings of fact also indicate that the law enforcement agencies which received the Alert Lists did not have a permissible purpose for the Lists as required by Section 604. Specifically, the Alert Lists were disseminated to the law enforcement agencies by Mr. Howard even though he was not instructed to do so by a court or the consumers whose names appeared on the lists, and these agencies did not use them in connection with the granting of credit, the underwriting of insurance, employment purposes, the provision of government licenses or benefits, or in connection with a business transaction with consumers whose names appeared on the lists. (IDJ at 22, 23.) Therefore, the Alert Lists were not released for any of the permissible purposes listed in either Section 604 or Section 608.

C. FAILURE TO OBTAIN CERTIFICATION AND VERIFICATION

The ALJ found that Mr. Howard did not obtain from subscribers or law enforcement agencies any certification that the lists would be used only for the permissible purposes stated in the FCRA, nor did he verify that the lists were only being used for such purposes. (IDJ at 24.) In addition, Mr. Howard and his representatives did not at any time ask subscribers what they intended to do with the lists or

[14] In this regard the Commission has previously stated:

[This interpretation] does not preclude the furnishing of information by a consumer reporting agency which is coded so that the consumer's identity will not be disclosed . . . . For example, unique identifiers such as social security number, driver's license number, or bank account number will provide adequate coding. 16 C.F.R. 600.1(e).

discuss with them any restrictions on the use of the lists. (IDJ at 25.) Finally, Mr. Howard did not require that subscribers state in writing what uses would be made of the lists or agree to restrict their uses of the Alert Lists. (IDJ at 26.) Through such omissions, respondent Ralph Howard violated Section 607 of the FCRA.

D. FAILURE TO ASSURE ACCURACY OF CONSUMER REPORTS

Section 607(b) of the FCRA requires consumer reporting agencies to utilize reasonable procedures to assure the maximum possible accuracy of the information contained in consumer reports. The ALJ found that, prior to placing a consumer's name on the Alert List, Mr. Howard had no way of knowing whether all the names submitted by subscribers were individuals whose checks had in fact been dishonored. (IDJ at 27.) More significantly, an individual's name appeared on successive lists until a subscriber notified Mr. Howard that the name should be deleted. (IDJ at 28.) [13]

As noted above, there were two mechanisms employed by Mr. Howard to delete names from the lists: delete cards and audit lists. *See* p. 3, *supra*. Both systems were inadequate inasmuch as Mr. Howard did not require the subscribers to agree in writing to send in delete cards and did not impose penalties on subscribers for failing to submit delete cards or audit lists on a timely basis. (IDJ at 30-31.) Mr. Howard had no system for determining whether each subscriber submitted the delete cards and audit sheets. *Id.* Indeed, the only mechanism for uncovering errors in the system consisted of contacts from consumers complaining that their names had erroneously appeared on the Alert Lists. (IDJ at 31.)

In sum, the record in this proceeding establishes that Mr. Howard employed only token procedures to detect errors in reporting information on the Alert Lists. Such procedures are insufficient to meet the requirements of Section 607(b) that reasonable procedures be followed to assure maximum possible accuracy of the information contained in consumer reports.

E. SALE OF FRANCHISES

In his initial decision, the ALJ found that respondent Howard Enterprises is engaged in the business of selling Alert List franchises. (IDJ at 4-5.)[15] He also found that the manner in which the

[15] The ALJ's findings of fact also establish that the sale and operation by respondents of Alert List franchises are in or affecting interstate commerce. (IDJ at 6-10.) *See, e.g., NLRB* v. *Reliance Fuel Oil Corp.*, 371 U.S. 224 (1963); *Local 167 of the International Brotherhood of Teamsters* v. *United States*, 291 U.S. 293, 297 (1934); *FTC* v. *Pacific States Paper Trade Association*, 273 U.S. 52 (1927); *Seligson* v. *Plum Tree, Inc.*, 361 F. Supp. 748, 751 (E.D. Pa. 1973.)

franchisees operate their Alert List systems was virtually identical to the way Mr. Howard operated his system. (IDJ at 12.) This finding is supported by the substantial influence which Mr. Howard and Howard Enterprises maintained over the business operations of their franchisees. The evidence indicates that, while establishing their systems, franchisees were trained and assisted by Mr. Howard. (*See* Tr. 223, 227, 318.) The computer program which franchisees used in operating their systems was supplied by Howard Enterprises (Tr. 22, 226–27, 229, 318) and could not be altered by franchisees unless Howard agreed. (Tr. 119, 317–18). Additionally, respondents supplied forms and promotional material to franchisees. (Adm. 69.)

Section 621(a) of the FCRA provides that a violation of any requirement or prohibition imposed under the FCRA constitutes an unfair or deceptive act or practice in violation of Section 5 of the FTC Act. It is a well-settled principle that one who places in the hands of another the means or instrumentality to engage in [14] an unfair or deceptive act or practice has thereby violated Section 5 of the FTC Act. *See, e.g., FTC* v. *Winstead Hosiery Co.,* 258 U.S. 483, 494 (1922). This principle was recently applied by the Commission in *National Housewares, Inc.,* 90 F.T.C. 512, 590 (1977) to hold respondents liable for unfair and deceptive treatment of consumers by independent distributors of respondents' products. As a factual basis for its holding, the Commission cited that respondents had provided distributors with a particular sales method, had advised and encouraged distributors to use practices which were deceptive, and had supplied materials to implement the method. *Id.*

This legal standard has been recognized in a variety of other, analogous, circumstances. *See, e.g., Benrus Watch Co.* v. *FTC,* 352 F.2d 313, 318 (8th Cir. 1965); *Regina Corp.* v. *FTC,* 322 F.2d 765, 768 (3d Cir. 1963); *C. Howard Hunt Pen* v. *FTC,* 197 F.2d 273, 281 (3d Cir. 1952).

The record in this proceeding demonstrates that, by selling Alert List franchises, respondents have provided the means for others to engage in unfair and deceptive practices. As we discussed above, Alert List systems, by their very nature, are violative of the FCRA. The lists disseminate far more consumer credit information than subscribers are entitled to, fail to provide for the required certification and verification, and are not operated in such a way as to assure maximum possible accuracy. In addition, the training and assistance provided to franchisees by respondents, which resulted in methods of operation almost identical to those of Mr. Howard found to be illegal above, support respondents' liability. By franchising a business methodology which is inherently illegal under the FCRA, respondents have violated Section 5 of the FTC Act.

Because respondents are responsible for setting in motion the FCRA violations by franchisees, it is appropriate to reach the practices of all Alert List system operators through them. Our goal is to bring the entire network of Alert List systems into compliance with the statutory requirements of the FCRA. To that end, the order issued with this opinion requires not only that respondents themselves comply, but that they obtain compliance from their franchisees.[16] [15]

V. CONSTITUTIONALITY OF THE FCRA

Respondents assert that enforcement of the FCRA will unconstitutionally deprive them of their right under the First Amendment to free speech and press. (RAB at 11.) Although respondents purport to be challenging only the application of the FCRA to them, their arguments in effect challenge the constitutionality of the statute on its face. (RAB at 11–14.)

While administrative agencies are often called upon to determine whether particular applications of the laws they administer comport with the Constitution, there is considerable case law support for the view that an administrative agency does not have authority to determine the constitutionality of the statutes it enforces.[17] Such precedent is rooted in a recognition that administrative agencies are created to enforce the law and effect the legislative mandate.

> Were an agency to conclude that a duly enacted statute was unconstitutional, it might thereby preclude any review of that issue by the courts, thus thwarting a constitutional scheme which contemplates passage of laws by Congress, enforcement of them by the executive, and ultimate determination of their constitutionality by the judiciary. *Verrazzano Trading Corp., et al.*, 91 F.T.C. 888, 952 (1978).

At the same time, however, the Commission has recognized that there may be persuasive reasons justifying consideration of constitutional issues by administrative agencies, arising out of both the obligation of each Commissioner to "support and defend the Constitution" and of the expertise of the agency in construing the statutes it enforces, as the result of which it may be in the best position to

[16] As a practical matter, because of the degree of control Respondents exercise over the way franchisees conduct business, this should not prove burdensome. Once respondents alter their Alert List format and procedures, it will be a simple matter for franchisees to follow suit. However, to ensure full compliance with the FCRA, the order also requires respondents to discontinue their business relationship with any franchisee who fails to comply. (Paragraph II.C.) We note that, if necessary, this may be accomplished through terms of the franchise agreement allowing breach if franchisees engage in any practice "detrimental to the public."

[17] *See, e.g., Weinberg* v. *Salfi*, 422 U.S. 749, 765 (1975); *Johnson* v. *Robinson*, 415 U.S. 361, 368 (1974); *Public Utilities Comm'n* v. *United States*, 355 U.S. 534, 539 (1958); *Engineers Public Service Co.* v. *SEC*, 138 F.2d 936, 952–53 (D.C. Cir. 1943), dismissed as moot, 332 U.S. 788.

make the first assessment of their constitutionality. These considerations have led us to suggest that, where the underlying constitutionality of a statute is challenged, the best approach is that

> administrative agencies ought not blind themselves to constitutional considerations, but in taking them into account they should give extreme deference to the implicit view of Congress that such statutes are constitutional, so as to avoid thwarting the Congressional intent by precluding judicial review of a statute's constitutionality. *Verrazzano, supra,* 91 F.T.C. at 953.

[16] Here, as in *Verrazzano,* we are able to offer the perspective of our administrative experience as it relates to the constitutionality of the FCRA without precluding the opportunity for judicial review.

Respondents correctly point out that in recent cases the Supreme Court has recognized that commercial speech is not wholly beyond First Amendment protection. (RAB at 12, citing *Virginia State Board of Pharmacy* v. *Virginia Citizens' Consumer Council,* 425 U.S. 748 (1976); *Linmark Associates, Inc.* v. *Township of Willingboro,* 431 U.S. 85 (1977); and *Bates* v. *Arizona State Bar,* 433 U.S. 350 (1977).) However, it is clear from those cases that the Court does not, as respondents would have us do, equate commercial and noncommercial, or "political," speech. Indeed, in *Ohralik* v. *Ohio State Bar Ass'n,* 436 U.S. 447, 456 (1978), the Court expressly reaffirmed the "limited measure of protection" extended to commercial speech, explaining that

> to require a parity of constitutional protection for commercial and noncommercial speech alike could invite dilution, simply by a leveling process, of the force of the Amendment's guarantee with respect to the latter kind of speech.

The Court in *Ohralik* also observed that commercial speech "occurs in an area traditionally subject to government regulation," and recognized that regulation of commercial speech is subject to a lower level of judicial scrutiny. *Id.* The approach taken by the courts in such situations has been one of balancing the First Amendment interests of the commercial speaker against countervailing justifications for the regulation. *See, e.g., Virginia State Board of Pharmacy* v. *Virginia Citizen's Consumer Council, supra; Linmark Associates, Inc.* v. *Township of Willingboro, supra;* and *Bates* v. *Arizona State Bar, supra.* Respondents discuss this test, but conclude that "no balancing of interest can remove the protection . . . ." (RAB at 14.)

While the FCRA does not in any sense remove the protected interest which Respondents have in disseminating Alert Lists, we believe that the FCRA will withstand their constitutional challenge. First, unlike the regulations at issue in *Virginia State Board, Linmark,* and *Bates,* the FCRA does not impose an absolute prohibition on dissemination of commercial information; it merely requires that the sensitive information in consumer credit reports be handled responsibly. Thus, the FCRA requirements may be seen as reasonable "time, place and manner" restrictions on commercial speech which have been held to be constitutional. *See, e.g., Bates, supra,* at 384. Moreover, the restrictions the statute placed on [17] dissemination of consumer reports appear to be clearly justified by the interests Congress expressed in ensuring the accuracy of credit information and protecting individuals' constitutional right to privacy.[18]

VI. Conclusion

To remedy the violations found, the Commission hereby enters the attached order.

Synopsis of Determinations for Purposes of 15 U.S.C. 45(m)(1)(B)

Howard Enterprises, Inc., et al. Docket 9096

1. It is unlawful under the Fair Credit Reporting Act (15 U.S.C. 1681, *et seq.*), and therefore an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45) for any consumer reporting agency[1] to disseminate consumer reports[2]

(a) to third parties which do not have a legitimate business need for the information in connection with a business transaction involving the consumer reported on;[3]

(b) to law enforcement agencies except to the extent authorized by Sections 604 and 608;

(c) without obtaining from prospective users written certification that the information will only be used for the permissible purposes stated in the FCRA, and then verifying that only such uses will be made of the information; and

[18] This analysis and conclusion are supported by a pre-*Virginia State Board* decision in which the Eighth Circuit ruled that certain provisions of the FCRA are constitutional based on a balancing of interests. *See Millstone* v. *O'Hanlon Reports, Inc.*, 528 F.2d 829, 833 (8th Cir. 1976).

[1] Section 603(b) of the FCRA defines a "consumer reporting agency" as any person who, by means of interstate commerce, regularly assembles or evaluates specified consumer credit information and disseminates it to third parties for a fee.

[2] "Consumer reports" include the information on "bad check lists" sold to assist merchants in deciding whether or not to accept checks from their customers, as well as other communications defined in FCRA Section 603(d).

[3] This standard does not preclude the furnishing of such lists if they are encoded through the use of unique identifiers other than names, such as social security numbers or bank account numbers, so that a user can determine the identity of any consumer reported on only through use of additional information provided by the consumer at the time of the transaction.

(d) without following reasonable procedures to assure maximum possible accuracy of the information contained in consumer reports.

2. It is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45) to sell a franchise which provides the means for third parties to engage in unfair and deceptive acts or practices.

Final Order

This matter having been heard by the Commission upon the appeal of complaint counsel from the initial decision and upon briefs in support thereof and opposition thereto, and the Commission, for the reasons stated in the accompanying opinion having substantially granted the appeal; therefore

It is ordered, That pages 1 to 15 of the initial decision of the ALJ be, and they hereby are, adopted as Findings of Fact of the Commission, except to the extent inconsistent with the Commission's findings of fact and conclusions of law contained in the accompanying opinion.

Other findings of fact and conclusions of law of the Commission are contained in the accompanying Opinion.

It is further ordered, That the following order to cease and desist be, and it hereby is, entered:

Part I

It is ordered, That respondent Ralph R. Howard, his agents, representatives, employees, successors, and assigns, directly or indirectly through any corporation, subsidiary, division or other device, in connection with the collecting, preparing, assembling and/or furnishing of consumer reports, as "consumer report" is defined in Section 603(d) of the Fair Credit Reporting Act (Pub. Law 91-508, 15 U.S.C. 1681, *et seq.*), and interpreted in the accompanying Opinion of the Commission, shall cease and desist from: [2]

A. Furnishing any consumer report to any person, unless such report is furnished:

1. In response to the order of a court having jurisdiction to issue such order; or

2. In accordance with the written instructions of the consumer to whom the report relates; or

3. To a person which respondent has reason to believe intends to use the information:

a. In connection with a credit transaction involving the consumer on whom the information is to be furnished and involving the extension of credit to, or review or collection of an account of, the consumer; or

b. For employment purposes; or

c. In connection with the underwriting of insurance involving the consumer; or

d. In connection with a determination of the consumer's eligibility for a license or other benefit granted by a governmental instrumentality required by law to consider an applicant's financial responsibility or status; or

e. In connection with a legitimate business need for the information in connection with a business transaction involving each consumer reported upon.

B. Furnishing "Alert Lists," or any other list, index, or compilation of consumer reports, unless encoded in such a way that a user can determine the identity of any consumer reported on only through the use of additional information and identification to be provided by the consumer at the time of the transaction with the user.

C. Failing to maintain reasonable procedures necessary to limit the furnishing of consumer reports to the purposes listed under Section 604 of the Fair Credit Reporting Act, as required by Section 607(a) of the Fair Credit Reporting Act, including, but not necessarily limited to, procedures: [3]

1. requiring prospective users of consumer reports to identify themselves,
2. requiring prospective users of consumer reports to certify the purposes for which the information in such reports is sought,
3. requiring prospective users of consumer reports to certify that the information in such reports will be used for no other purposes than those which have been certified,
4. verifying the identity of new prospective users of consumer reports prior to furnishing consumer reports to such users, and
5. verifying the uses certified by prospective users of consumer reports prior to furnishing consumer reports to said users.

D. Furnishing consumer reports to persons under circumstances in which there are reasonable grounds for believing that such reports will not be used for purposes listed in Section 604 of the Fair Credit Reporting Act.

E. Failing to follow reasonable procedures to assure maximum possible accuracy of information concerning the individuals to whom consumer reports relate, as required by Section 607(b) of the Fair Credit Reporting Act, including but not necessarily limited to, procedures:

1. to ensure with reasonable certainty that information about consumers is accurate before placing it on "Alert Lists" or other such compilations;

2. to ensure that prospective users provide prompt notice as to information which is no longer accurate and therefore should be deleted from the "Alert List" or other compilation, and

3. requiring prospective users to agree in writing to comply with the procedures described in E.2, above.

F. Failing to include the following statement on a fact sheet to be included with any "Alert List" or other consumer reports published and distributed by respondent, with such conspicuousness and clarity as is likely to be read and understood by users of such consumer reports:

The following information is subject to the Fair Credit Reporting Act which regulates use of consumer reports. It must be used for the following permissible purposes and no other: [4]

(1) In connection with a credit transaction involving the consumer on whom the information is to be furnished and involving the extension of credit to, or collection of an account of, the consumer; or

(2) In connection with employment purposes; or

(3) In connection with the underwriting of insurance involving the consumer; or

(4) In connection with a determination of the consumer's eligibility for a license or other benefit granted by a governmental instrumentality required by law to consider an applicant's financial responsibility or status; or

(5) In connection with a legitimate business need for the information in connection with a business transaction involving the consumer.

The Fair Credit Reporting Act, Public Law 91-508, Section 619, states "Any person who knowingly and willfully obtains information on a consumer from a consumer reporting agency under false pretenses shall be fined not more than $5,000 or imprisoned not more than one year, or both."

PART II

It is further ordered, That respondents, Howard Enterprises, Inc., its successors and assigns, and its officers, and Ralph R. Howard, individually and as an officer of Howard Enterprises, Inc., and respondents' agents, representatives, employees, successors, and assigns, directly or indirectly through any corporation, subsidiary, division, or other device, in connection with the sale, or offering for sale, of franchises, licenses, or business opportunities provided by respondents to others, and in connection with respondents' continuing business relationships with such others, in or affecting commerce, as commerce is defined in the Federal Trade Commission Act, shall:

A. Cease and desist from selling or providing in any manner franchises, licenses, or business opportunities (hereinafter referred to in Section II of this order as "franchises") to others to engage in the collecting, preparation, assembling or furnishing of consumer reports, as "consumer report" is defined in Section 603(d) of the Fair Credit Reporting Act and interpreted in the accompanying opinion of the Commission, unless respondents (1) obtain written agreements from the purchasers or recipients of franchises (hereinafter referred to in Section II of this order as "franchisees") in which the franchisees agree to conform their practices to the requirements of Section I of this order, (2) retain copies of such agreements during the period of any business relationship with the franchisees, and (3) make such agreements available for inspection and copying on request by Commission representatives.

B. (1) Obtain from each of the respondents' franchisees existing in such capacity on the day this order is served on respondents, the written agreements of the franchisees to conform their practices to the requirements of Section I of this order, (2) retain copies of such agreements during the period of any business relationship with the said franchisees, and (3) make such agreements available for inspection and copying on request by Commission representatives.

C. Discontinue any further business relationship with any franchisee described in paragraph II.B. above which has failed to comply with paragraph II.B. within sixty (60) days of the service of this order upon respondents.

D. Discontinue any further business relationship with any current or future franchisee which fails to comply with the terms of Section I of this order.

PART III

It is further ordered, That respondents Ralph R. Howard and Howard Enterprises deliver a copy of this order to cease and desist to all present and future employees of said respondents engaged in the preparation and/or furnishing of consumer reports, and that said respondent secure a signed statement acknowledging receipt of said order from all such personnel.

Part IV

It is further ordered, That respondents deliver a copy of this order and a copy of the Fair Credit Reporting Act to each of their present franchise or license holders within thirty days, to all future franchise or license holders, and to any entity connected with said respondents who distribute consumer reports as "consumer report" is defined in Section 603(d) of the Fair Credit Reporting Act and interpreted in the accompanying opinion of the Commission.

Part V

It is further ordered, That respondents notify the Commission at least thirty days prior to any proposed change in the corporate respondent, such as dissolution, assignment or sale resulting in the emergence of a successor corporation or corporations, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of the order.

Part VI

It is further ordered, That the respondents herein shall, within sixty days after service of this order, file with the Commission a written report setting forth in detail the manner and form of their compliance with this order.

IN THE MATTER OF

FEDDERS CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2971. Complaint, June 14, 1979 — Decision, June 14, 1979*

This consent order, among other things, requires an Edison, N.J. manufacturer and distributor of various products, including split system heat pumps, to offer, without charge, a replacement defrost cycle switch to all current owners of split system heat pumps manufactured by Fedders between November, 1975 and June 1, 1978; to extend a full warranty on the sealed system of the heat pump until May 1, 1980 to those purchasers who elect installation of the new defrost switch; and to reimburse all past or current owners of the affected heat pumps for any repair to the sealed system of the unit for which the owner has paid. The company must mail notices to current and past owners of the affected heat pumps to let them know about the remedial program, and advertise the program in national magazines if a sufficient number of owners cannot be reached by letters.

Appearances

For the Commission: *Robert S. Blacher* and *Gary M. Laden.*

For the respondent: *Benjamin Zelenko,* Washington, D.C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Fedders Corporation, a corporation, hereinafter sometimes referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. For the purposes of this complaint, the following definitions shall apply:

"Split system heat pump" shall mean a central residential heating/cooling air conditioner having a condenser section installed out-of-doors which includes an air pressure defrost cycle switch and a matching evaporator section installed indoors manufactured by

* Reported as modified by Commission order dated August 8, 1979.

Fedders Corporation between November 1, 1975 and June 1, 1978 under the brand names "Fedders Model CKH" or "Climatrol."

"Hermetic system" shall mean the compressor, condenser, evaporator, reversing valve and interconnecting tubing.

A "defect" in a product or component thereof occurs if the product or component thereof is subject to or potentially subject to a significant number of failures in normal operation, including failures occurring under operating conditions that either are within the parameters specified by the manufacturer or reflect reasonably expected ordinary abuse of or failures to maintain the product. For purposes of this definition, failures attributable to normal deterioration of a component as a result of age and wear are excluded.

PAR. 2. Respondent Fedders Corporation is a corporation organized, existing, and doing business under and by virtue of the laws of the State of New York, with its principal office and place of business located at Woodbridge Ave., Edison, New Jersey.

PAR. 3. Respondent is now, and has been, engaged in the manufacture, offering for sale, sale or distribution of split system heat pumps.

PAR. 4. In the course and conduct of its aforesaid business, respondent causes the said split system heat pumps, when sold, to be transported from its place of business located in various States of the United States to distributors thereof located in various other States of the United States and in the District of Columbia. Respondent maintains, and at all times mentioned herein has maintained, a substantial course of trade in said products in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 5. On or about February 23, 1978, and before, respondent received information by which it knew, or had reason to believe that there was a defect in the hermetic system of split system heat pumps manufactured by respondent. At such time, respondent received information by which it knew, or had reason to believe that the hermetic system failure was attributable to improper operation of the air pressure switch that regulates the defrost cycle of the compressor. Respondent knew, or had reason to believe, that the air pressure switch operated improperly under weather conditions that respondent could reasonably expect to be encountered with such split system heat pumps. Respondent knew, or had reason to believe, that improper operation of the air pressure switch caused inadequate defrosting of the hermetic system leading to inadequate lubrication of such system and eventual failure in a significant number of instances.

PAR. 6. Respondent has represented, directly or by implication, by and through the offering for sale of its split system heat pumps, that its split system heat pumps do not have any latent defect which substantially affects the reliability, durability, or performance of such split system heat pumps.

PAR. 7. In truth and in fact, in a significant number of instances, respondent's split system heat pumps suffer or may suffer failure of the hermetic system which substantially affects the reliability, durability, or performance of such split system heat pumps. Therefore, said representations were and are unfair or deceptive.

PAR. 8. Notwithstanding its knowledge of the improper operation of the air pressure switch regulating the defrost cycle, respondent is failing and has failed to disclose to ultimate purchasers of split system heat pumps information concerning the possibility of substantial damage to the hermetic system of such heat pumps and the nature and extent of repairs which may be necessary to correct such problem. Respondent therefore is failing and has failed to disclose material facts which, if known to prospective purchasers, would be likely to affect their consideration of whether to purchase a split system heat pump from respondent. Failure to disclose the aforesaid facts to current owners of split system heat pumps has caused them substantial economic harm due to inability on their part to avoid or prevent substantial damage to the hermetic system of their split system heat pumps and to avoid paying for unnecessary repairs that do not correct the problem. Such failures to disclose are deceptive or unfair acts or practices.

PAR. 9. The use by the respondent of the aforesaid acts and practices has had, and now has, the capacity and tendency to mislead members of the consuming public who are purchasing and have purchased a substantial number of split system heat pumps equipped with the improperly operating air pressure switch regulating the defrost cycle.

Therefore, the aforesaid acts and practices of respondent, as herein alleged, were and are all to the prejudice and injury of the public and constitute unfair or deceptive acts or practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Bureau of Consumer

Protection proposed to present to the Commission for its consideration and which if issued by the Commission would charge respondent with violation of the Federal Trade Commission Act, as amended; and

The respondent, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, make the following jurisdictional findings and enters the following order:

1. Respondent Fedders Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located at Woodbridge Ave., in the City of Edison, State of New Jersey.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

I

It is ordered, That respondent Fedders Corporation, a corporation, its successors and assigns, and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with the manufacture, offering for sale, sale or distribution of split system heat pumps in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, shall forthwith:

1. Make available, without charge, to each distributor or dealer

of respondent's split system heat pumps a sufficient quantity of time defrost system service kits, as described in respondent's Field Bulletin - Service dated June 5, 1978 (Publ. No. 23-65-0037N-001), to replace, as necessary pursuant to this order, the air pressure defrost cycle switches on split system heat pumps sold or distributed by respondent, and offer reasonable reimbursement for labor costs to each distributor or dealer for installation of the time defrost system service kits;

2. Offer to each current owner of a split system heat pump the option to have installed, without charge for parts or labor, the time defrost system service kit described in paragraph one (1) of this section, and install such time defrost system service kit, without charge for parts or labor, within ninety (90) days after receiving notice from such current owner that the owner has elected installation of the time defrost system. Each such current owner shall be sent, within ten (10) days after the date this order becomes final, pursuant to the procedures set forth in Section II of this order, notice of the option provided by this paragraph and a pre-addressed, postage-paid card by which to elect installation of the time defrost system. The notice of the option provided by this paragraph shall be as set forth in Appendix (A) of this order. The card by which to elect installation of the time defrost system shall be as set forth in Appendix (B) of this order. Failure of any current owner or addressee to whom such notice has been mailed, and which has not either been returned as undeliverable or notice of non-delivery provided by the postal service, to return such card within sixty (60) days of the date of mailing shall be considered an election not to have the time defrost system service kit installed;

3. Extend to each current owner of a split system heat pump who, pursuant to paragraph two (2) of this order, elects to have installed the time defrost system service kit, and to each current owner of a split system heat pump to whom notice of the option provided by paragraph two (2) of this order has not been mailed or has been mailed pursuant to Sections II (A) or (B) and has either been returned as undeliverable or notice of non-delivery provided by the postal service, a "full warranty" that meets the Federal minimum standards for warranty set forth in, and otherwise complies with, the Magnuson-Moss Warranty - Federal Trade Commission Improvements Act, 15 U.S.C. 2301, *et seq.,* and regulations promulgated thereunder. The warranty required by this paragraph shall cover any defect in material or workmanship of the hermetic system (including compressor) of the split system heat pump and shall be without charge for parts or labor. The warranty required by this

paragraph shall be effective until May 1, 1980. Such warranty shall extend to any person to whom the split system heat pump is transferred during the duration of the warranty. Each current owner of a split system heat pump shall be sent, within ten (10) days after the date this order becomes final, pursuant to the procedures set forth in Section II of this order, a copy of the warranty required by this paragraph. The warranty shall be as set forth in Appendix (C) of this order;

4. Provide to all owners of split system heat pumps reimbursement for all payments, incurred by such owners from date of installation of such split system heat pump until ninety (90) days after the date this order becomes final, in connection with any repair to the hermetic system (including compressor) of such split system heat pump. Reimbursement shall be for all such payments, covering both parts and labor. Notice of the right to reimbursement shall be provided to all past or current owners of split system heat pumps and shall be mailed pursuant to the procedures set forth in Section II of this order. The notice of the right to reimbursement shall be as set forth in Appendix (A) of this order. Proof of entitlement to reimbursement shall be by affidavit, as set forth in Appendix (D) of this order, accompanied by either (1) a cancelled check, or (2) an invoice, receipt, work order, purchase order, or similar document which gives evidence that the repair was made and paid for by the owner. The respondent shall pay, without further verification and without dispute, within forty-five (45) days after receipt, any claim for reimbursement where the proof of entitlement required by this paragraph has been provided. The respondent need not pay any claim for reimbursement under this paragraph if mailed later than sixty (60) days after such owner or addressee has been mailed notice of the right to reimbursement which has not been either returned as undeliverable or notice of non-delivery provided by the postal service.

II

A. *It is further ordered,* That respondent shall mail, within ten (10) days after the date this order becomes final, to all owners of split system heat pumps who can be identified through respondent's dealer-distributor network, the following "consumer notice" package:

1. The letter as set forth in Appendix (A) of this order providing notice of the right to have installed the time defrost system service kit, the extended full warranty on the hermetic system (including

compressor), and the right to reimbursement for repair payments, as provided in paragraphs 2, 3 and 4 of Section I of this order;

2. A pre-addressed, postage-paid card by which the current owner may elect installation of the time defrost system service kit pursuant to paragraph two (2) of Section I of this order, as set forth in Appendix (B) of this order;

3. A copy of the extended full warranty on the hermetic system (including compressor) pursuant to paragraph (3) of Section I of this order, as set forth in Appendix (C) of this order;

4. An affidavit for proof of entitlement to reimbursement for repair payments pursuant to paragraph four (4) of Section I of this order, as set forth in Appendix (D) of this order.

The "consumer notice" package shall be sent by third class, bulk rate, metered mail with the words " ADDRESS CORRECTION REQUESTED" and "RETURN POSTAGE GUARANTEED" printed in red ink on white background in 12-point boldface type in the upper left hand corner of the envelope. The return mailing address of the respondent shall also be printed in the upper left hand corner of the envelope. The envelope shall also prominently display in 12-point extra boldface type, printed in Cheltenham, Antique, Bodoni or Helvetica lettering, in red ink on white background, the words:

SPECIAL CONSUMER NOTICE

OUR RECORDS SHOW THAT YOU OWN (or used to own) A FEDDERS [CLIMATROL] HEAT PUMP. The defrost switch may need repair. Fedders [Climatrol] will fix it free, and may pay you back for some past repairs. Details inside.

B. *It is further ordered,* That respondent shall, for each "consumer notice" package mailed pursuant to subsection (A) above for which address correction has been provided by the postal service, mail, within ten (10) days after such correction has been received, by first class mail, the "consumer notice" package to:

1. The original address to which the "consumer notice" packag had been mailed, with the name of the original addressee delete and substitute therefor "RESIDENT" and

2. The corrected address provided by the postal service, with t name of the original addressee.

The envelope shall display, in the manner specified in subsection above, the words:

SPECIAL CONSUMER NOTICE

OUR RECORDS SHOW THAT YOU OWN (or used to own) A FEDDERS [CLIMATROL] HEAT PUMP. The defrost switch may need repair. Fedders [Climatrol] will fix it free, and may pay you back for some past repairs. Details inside.

C. *It is further ordered,* That respondent shall, within thirty (30) days after the date this order becomes final, file with the Commission a copy of the mailing list of owners of split system heat pumps to whom the "consumer notice" package has been mailed pursuant to subsection (A) above and has not been returned, and a copy of a receipt from the postal service showing the total number of pieces received for mailing.

D. *It is further ordered,* That respondent shall, within ninety (90) days after the date the Commission or its representative notifies respondent of the manner of selecting addresses to be inspected, conduct an on-site inspection at one (1) percent of the addresses to which the "consumer notice" package has been mailed pursuant to subsection (A) above and has not been returned in order to verify that such addressee is in possession of a split system heat pump. The addresses to be inspected shall be chosen at random in a manner selected by the Commission or its representative. Any mailing to an address selected for inspection which is returned during the inspection period shall be taken off the list of addresses to be inspected without necessity of substitution, and shall not be included in the calculations pursuant to Section III(A). The results of such inspections shall be filed with the Commission in the form of an affidavit, signed by an officer of the respondent, within ninety (90) days after the date the Commission or its representative notifies respondent of he manner of selecting addresses to be inspected. The affidavit shall how the total number of inspections and the total number of ddressees who are not in possession of a split system heat pump. The fidavit shall show the name from the mailing list and address for ch site inspected. The affidavit shall also show the number of ilings returned as specified in Sections III(A)(2) and (3).

III

It is further ordered, That respondent shall, within twenty (20) after the date the Commission or its representative notifies it of lure to mail the "consumer notice" package to ninety (90) nt of the current owners of split system heat pumps, place for vailable publication, in the national editions of the periodicals listed in Appendix (E) of this order, in a size of not less than one-half (1/2) page, or two (2) full columns if half-page is unavailable, of the periodical in which the advertisements are inserted, both of the "recall advertisements" as set forth in Appendices (F) and (G) of this order in the style, type, and format as depicted therein.

Provided However, respondent is not required to place both of the "recall advertisements" set forth in Appendices (F) and (G) of this Order, if it places one advertisement in each of the periodicals listed in Appendix (E) of this Order which advertisement refers to both Fedders and Climatrol, contains language identical to that in the "recall advertisements" set forth in Appendices (F) and (G), except that reference is made to both Fedders and Climatrol heat pumps, and meets all other requirements set forth in Section III, and Appendices (E), (F) and (G) of the Order.

Provided however, that the recall advertisements ordered pursuant to this Section shall not be required if respondent mails the "consumer notice" package pursuant to Section II(A) to ninety (90) percent of the current owners of split system heat pumps. The percentage of current owners to whom notice has been mailed shall be calculated on the basis of:

1. The number of mailings pursuant to Section II(A) as evidenced by the receipt from the postal service showing the total number of pieces received for mailing as required by Section II(C); *minus*
2. The number of mailings pursuant to Section II(A) that were returned as undeliverable with no address correction provided by the postal service and that were not mailed again to "Resident" as provided in Section II(B)(1); *minus*
3. The number of mailings returned as undeliverable that were mailed pursuant to Section II(B)(1); and *minus*
4. The number of addressees who are not in possession of a split system heat pump based on projection from the sample of on-sit inspections carried out pursuant to Section II(D) of this order. Tho not now in possession of a split system heat pump shall be presum not to have possessed such a unit since November 1, 1975 unless respondent can establish otherwise. It is hereby agreed that margin of error for this sampling is five (5) percent.

A sample calculation pursuant to this section is set fort Appendix (H) of this order.

B. *It is furthered ordered,* That respondent shall ma "consumer notice" package as set forth in Section II(A) to any of split system heat pumps who responds within three (3) mc the last publication of any advertisement required by this

IV

For purposes of this order:

1. "Split system heat pumps" shall mean a central residential heating/cooling air conditioner having a condenser section installed out-of-doors which includes an air pressure defrost cycle switch and a matching evaporator section installed in-doors manufactured by Fedders Corporation between November 1, 1975 and June 1, 1978 under the brand names "Fedders Model CKH" or "Climatrol."

2. "Current owners" shall include all persons who own or are in possession of split system heat pumps as of the date this order becomes final (but not including dealers or distributors), and shall not be limited to original purchasers.

"Owners" and "past owners" shall also not be limited to original purchasers, and shall also not include dealers or distributors.

3. "Hermetic system" or "sealed system" shall mean the compressor, condenser, evaporator, reversing valve and interconnecting tubing.

V

A. *It is further ordered,* That respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of this order.

B. *It is further ordered,* That respondent shall maintain all ecords that relate to any compliance obligations arising out of this ·der for a period of not less than three (3) years and shall make ch records available to the Commission or its representative upon ıuest.

'. *It is further ordered,* That the respondent herein shall within hundred (200) days after service upon them of this order, file the Commission a report, in writing, setting forth in detail the ıer and form in which it has complied with this order.

NDIX (A): [CONSUMER NOTICE]

CONSUMER NOTICE

ers [Climatrol] Heat Pump Owner:

rds show that you own, or used to own, a Fedders [Climatrol] Heat Pump. these units, the defrost switch may need repair. Some of these units have ʒ up due to extremely cold and damp weather.

ONLY SPLIT SYSTEM HEAT PUMPS HAVE THE PROBLEM

Take a look at your unit. If it's part indoors and part outdoors, it's a split system.

FEDDERS [CLIMATROL] WILL FIX YOUR HEAT PUMP. FREE.

We have a new defrost switch which we think will fix the problem. We will install it without charge. All you have to do is return the enclosed card marked "YES" and we will contact you to install the switch.

A NEW WARRANTY, TOO.

If you have the switch replaced, you'll get an extended *full* warranty that protects the sealed system of your heat pump until May 1, 1980. The warranty covers parts and labor. It is in addition to the warranty you received when you purchased your heat pump. A copy of the warranty is enclosed. If you do not elect to install this switch, your original warranty will continue to apply.

WHAT YOU MUST DO

You *must* return the enclosed card to have the defrost cycle switch replaced. If you do not return the card, you will not get this warranty.

PAID FOR REPAIRS? FEDDERS [CLIMATROL] PAYS YOU BACK.

If you have already paid for repairs to the sealed system, we will pay you back. *Even if you no longer own the unit or the home in which it is installed,* we will still pay you back.

This includes repairs to the sealed system only. Included are the compressor, condenser, evaporator, reversing valve and interconnecting tubing.

You must fill out the enclosed affidavit. Attach proof that you paid for repairs. A cancelled check will do. Even better proof is some kind of receipt that shows repairs were made and you paid for them. The affidavit has full instructions. You must have the affidavit notarized. Most banks have a notary public who will do this for about 50 cents.

ACT NOW. You must return the enclosed card within sixty (60) days. And, if you have paid for repairs, you must return the enclosed affidavit within sixty (60) days for us to pay you back. The sixty (60) days starts to run from the date we *mailed* you this letter. So don't delay.

If you have any questions, you can call us during business hours at (201) 494-8802.

Sincerely,
Consumer Affairs Department
Fedders Corporation
[Climatrol Sales Company]
Edison, New Jersey 08817

APPENDIX (B): [Card by which to elect installation of the defrost system service kit]

PLEASE TYPE OR PRINT CLEARLY

Name ____________________

Address ____________________
Street City State Zip Code

Telephone ( ) __________

MARK ONE:

( ) *Yes.* I want the *free* switch replacement and the extended full warranty on the sealed system.

( ) No. I do not want the switch replacement. I understand that I will not get the extended warranty.

If you have already had the switch replaced, please mark *Yes* and put a mark here, too.( ) If you have already had the switch replaced, the switch will not be replaced again but you do get the extended warranty. If you are not sure whether the switch was replaced, call your local Fedders [Climatrol] dealer or repair company.

APPENDIX (C): [Extended Full Warranty]

EXTENDED FULL WARRANTY ON "SEALED SYSTEM" UNTIL MAY 1, 1980

WHAT IS COVERED

This warranty is for "split system" heat pumps. It covers the sealed system of the ʰeat pump. This includes the compressor, condenser, evaporator, reversing valve and nterconnecting tubing.

ʼHAT WE PROMISE

Fedders will repair or replace any part of the sealed system that is defective. You 'l not be charged for parts, labor, or anything else. If we are unable to fix the sealed tem of your heat pump after a reasonable number of attempts, you have a right to ll refund or a free replacement of the heat pump.

ΛT IS NOT COVERED

ιis warranty does not include consequential or incidental damages *except* damage y part of the heat pump that results from any defect covered by this warranty. *states do not allow the exclusion or limitation of consequential or incidental ʒes, so the above limitation or exclusion may not apply to you.*

.ONG THIS WARRANTY LASTS

! May 1, 1980. Implied warranties on the sealed system of your heat pump will ɪs long as is provided by state law starting from the date your original written ɣ became effective.

ƆOVERED

d anyone to whom ...

WHAT YOU MUST DO

You *must* return the enclosed card to have the defrost cycle switch replaced. This replacement is free. If you do not return the card, you will not get this warranty. This warranty starts the day you mail the enclosed card.

For service under this warranty, contact your local Fedders [Climatrol] Authorized Service Company. Your dealer can give you the name and address of the one nearest you. Or call (800) 882-6500 for this information. This call is free, and is available 24 hours a day, 7 days a week.

If the Fedders [Climatrol] Authorized Service Company has not solved the problem, please contact us by mail or call during business hours.

Consumer Affairs Department
Fedders Corporation
[Climatrol Service Company]
Edison, New Jersey 08817
Telephone — (201) 494-8802

THIS WARRANTY GIVES YOU SPECIFIC LEGAL RIGHTS AND YOU MAY ALSO HAVE OTHER RIGHTS WHICH VARY FROM STATE TO STATE.

APPENDIX (D): [Affidavit for proof of entitlement to reimbursement for repair payments pursuant to paragraph four (4) of Section I]

AFFIDAVIT

Name ______________________________

Address ______________________________
Street

____
(City) (State) (Zip Code)

Telephone ______________________________

1. I own (or owned) a *Fedders* [Climatrol] heat pump. It is a split system heat pump. Part of the heat pump is outdoors. And part of it is indoors.

2. The model number on my heat pump is ______________. The serial number of my heat pump is ______________. NOTE: Both of these numbers can be found on a metal plate on the cabinet of the part of your unit that is outdoors.

3. I swear (or affirm) that I have paid for *repairs* to the *sealed system* of my heat pump. This includes repair or replacement of the compressor, condenser, evaporator, reversing valve and interconnecting tubing.

This includes only repairs or replacement of such parts. NOT included is routine maintenance.

4. ATTACH A COPY OF THE CANCELLED CHECK *OR* RECEIPT SHOWING THAT YOU PAID FOR REPAIRS. ATTACH A COPY OF ANYTHING YOU HAVE THAT SHOWS WHAT REPAIRS WERE MADE AND THAT *YOU* PAID FOR THE REPAIRS.

We will only pay you back if you attach a cancelled check *or* receipt.

If you have lost your receipt, try to get a copy from the person or company that made the repair.

FOR FASTEST REPAYMENT, ATTACH A CANCELLED CHECK *AND* A RECEIPT.

5. I have not signed a release or received any payment or reimbursement or made any other settlement with Fedders [Climatrol], any of its companies or representatives, any insurance company or anyone else in connection with the claim for reimbursement now made.

All of the above information is true and correct to the best of my knowledge.

________________ ________________

Date Signature

Subscribed and sworn to before me this __________ day of ______________ , 1978.

____

(Notary Public)
(SEAL)

APPENDIX (E): [List of periodicals in which both "recall advertisements" as required by Section III of this order shall be inserted for publication.]

1. Better Homes & Gardens
2. Newsweek
3. Parade Magazine
4. Sports Illustrated
5. T.V. Guide

APPENDIX (G): (CLIMATROL RECALL ADVERTISEMENT)

Special Consumer Notice

Climatrol Free Heat Pump Fix-up

The problem. Some of our split system heat pumps may be failing from the effects of extremely cold and damp weather.

Only split system heat pumps have the problem. Look at your unit. If it's part indoors and part outdoors, it's a split system

Climatrol will fix it. Free. We have a new switch to fix the problem. No charge. Call us.

A new warranty, too. Call us to have the switch replaced. If you do, you'll get an extended full warranty that protects the sealed system of your heat pump until May 1, 1980. The warranty covers parts and labor.

Paid for repairs? Climatrol will pay you back. If you have already paid for repairs resulting from this problem, Climatrol will pay you back. Even if you no longer own the unit or the home in which it is installed, you may still qualify. Call us.

Call for details. Climatrol wants to do things right. Call us. Toll Free. 800-000-0000

Climatrol®

Consumer Affairs Department

Edison, NJ 08817

APPENDIX (F): (FEDDERS RECALL ADVERTISEMENT)

Special Consumer Notice

Fedders
Free Heat Pump Fix-up

The problem. Some of our split system heat pumps may be failing from the effects of extremely cold and damp weather.

Only split system heat pumps have the problem. Look at your unit. If it's part indoors and part outdoors, it's a split system.

Fedders will fix it. Free. We have a new switch to fix the problem. No charge. Call us.

A new warranty, too. Call us to have the switch replaced. If you do, you'll get an extended full warranty that protects the sealed system of your heat pump until May 1, 1980. The warranty covers parts and labor.

Paid for repairs? Fedders will pay you back. If you have already paid for repairs resulting from this problem, Fedders will pay you back. Even if you no longer own the unit or the home in which it is installed, you may still qualify. Call us.

Call for details. Fedders wants to do things right. Call us. Toll Free. 800-000-0000

FEDDERS

Consumer Affairs Department
Edison, NJ 08817

APPENDIX (H): [Sample calculation, pursuant to Section III(A), of percentage of current owners to whom notice has been mailed]

EXAMPLE

A.	Total number of split system heat pumps sold to owners as of the date this Order becomes final	=	35,000
B.	Number of mailings pursuant to Section II(A)	=	34,250
C.	Number deliverable after both mailings (See Sections III(A)(2) and III(A)(3))	=	1,000
D.	Number of addresses inspected pursuant to Section II(D)	=	332
E.	Number of addresses inspected which do not have split system heat pump	=	33

Formula: $\dfrac{B-C}{A} \times 100 = X\%$

$$\frac{E}{D} \times 100 = Y\%$$

X%—Y%+5% [margin of error]=percentage of current owners

$$\frac{34{,}250 - 1{,}000}{35{,}000} \times 100 = 95\%$$

$$\frac{33}{332} \times 100 = 9.9\%$$

95%—9.9%+5% [margin of error]=90.1%

Percentage of current owners to whom notice has been mailed=90.1%

IN THE MATTER OF

THE PILLSBURY COMPANY, ET AL.

DISMISSAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket 9091. Complaint, Nov. 11, 1976 — Dismissal Order, June 15, 1979*

This order dismisses a complaint issued on November 11, 1976 charging a Minneapolis, Minn. manufacturer of food products with violating Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act by acquiring Fox Deluxe Foods, Inc., a Chicago, Ill. producer and seller of frozen pizza. The Commission dismissed the complaint on ground that the merger is not illegal since it is unlikely to have significant anticompetitive effect in the national market for frozen prepared pizza.

Appearances

For the Commission: *Roger J. Leifer, Joseph Tasker, Jr.* and *Patricia S. Bangert.*

For the respondent: *John French* and *Randy L. Miller, Faegre & Benson* and *Dwight H. Oglesby,* The Pillsbury Company, all of Minneapolis, Minn.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondents have entered into an agreement which, if consummated, would result in a violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), and that said agreement therefore constitutes a violation of Section 5(a)(1) of the Federal Trade Commission Act, as amended, (15 U.S.C. 45(a)(1), and the Federal Trade Commission having reason to believe that the above-named respondent The Pillsbury Company has acquired the above respondent Fox Deluxe Foods, Inc. in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45) and having found that a proceeding with respect to said violations is in the public interest, issues its complaint stating its charges as follows:

* Reported as amended by order of the administrative law judge dated June 17, 1977.

Definitions

(1) The term "The Pillsbury Company" as used herein means the Pillsbury Company and any parent companies thereof, and all of its subisdiaries, divisions, affiliates and the predecessors of any of the foregoing.

(2) The term "Fox Deluxe Foods, Inc." as used herein means Fox Deluxe Foods, Inc. and any parent companies thereof, and all of its subsidiaries, divisions, affiliates and the predecessors of any of the foregoing.

(3) The term "Frozen Prepared Pizza" means pizza which is cooked, processed or manufactured and frozen for sale.

The Pillsbury Company

(4) Respondent The Pillsbury Company (hereinafter "Pillsbury") is a Delaware corporation with its principal office at the Pillsbury Building, 608 Second Ave. South, Minneapolis, Minnesota.

(5) Pillsbury is a leading manufacturer and marketer of a wide range of food products, including prepared baking mixes, refrigerated dough products, flour and frozen prepared pizza.

(6) In its fiscal year ending May 31, 1976, Pillsbury had revenues in excess of $1.5 billion and net income in excess of $41 million. Pillsbury is among the two hundred largest United States corporations.

(7) In November 1975, Pillsbury entered the frozen pizza business by acquiring Totino's Finer Foods, Inc., a leading manufacturer and seller of frozen prepared pizza, with sales in excess of $39 million in its fiscal year ending October 31, 1975, which Pillsbury now operates as its frozen foods division. For its fiscal year ending October 31, 1976, Pillsbury's frozen food division had frozen prepared pizza sales in excess of $48 million. Retail sales of Pillsbury's frozen prepared pizza under the Totino's brand amounted to approximately $66.2 million for the fifty-two week period ending August 27, 1976, which makes Pillsbury the third largest frozen prepared pizza manufacturer in the United States.

(8) At all times relevant herein, Pillsbury has engaged and i engaged in commerce as "commerce" is defined in Section 1 of th Clayton Act, as amended, and the agreement between Pillsbury ar Fox set forth in Paragraph (13a) is a method of competition commerce as "commerce" is defined in Section 4 of the Fede Trade Commission Act, as amended.

Fox Deluxe Foods, Inc.

(9) Respondent Fox Deluxe Foods, Inc. (hereinafter "Fox") is an Illinois corporation with offices at 222 South Riverside Plaza, Suite 442, Chicago, Illinois.

(10) Before the acquisition set forth in Paragraph (13b), Fox manufactured or processed, and sold, food products including poultry, butter, eggs and frozen prepared pizza.

(11) In its fiscal year ended February 29, 1976, Fox had net sales of approximately $12.2 million, and assets in excess of $3.1 million. In that year, Fox had sales of frozen prepared pizza in excess of $7.3 million. Retail sales of Fox's frozen prepared pizza amounted to approximately $8.1 million for the fifty-two week period ending August 27, 1976, which made Fox the tenth largest frozen prepared pizza manufacturer in the United States, prior to its acquisition by Pillsbury set forth in Paragraph (13b).

(12) At all times relevant herein, Fox has engaged and is engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, and the agreement between Fox and Pillsbury set forth in Paragraph (13a) is a method of competition in commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended.

The Acquisition Agreement

(13a) On or about October 6, 1976, Pillsbury and Fox agreed in principle to the acquisition by Pillsbury of assets of Fox used in the production and sale of frozen prepared pizza (the "pizza assets"). On or about November 3, 1976, Pillsbury and Fox entered into an agreement which provides, *inter alia,* for the sale of the pizza assets 'n exchange for approximately $3 million worth of Pillsbury common tock. The practical result of the agreement, if consummated, would e the end of Fox's existence as an independent business entity.

The Acquisition

(13b) On or about November 15, 1976 Pillsbury acquired the pizza sets of Fox for approximately $3 million worth of Pillsbury nmon stock.

TRADE AND COMMERCE

Relevant Line of Commerce

t) The manufacture and sale of frozen prepared pizza is a rate, distinct and relevant line of commerce. Frozen prepared pizza is one of the largest and fastest growing of all retail food sales categories. Calendar 1975 national retail frozen prepared pizza sales were estimated at approximately $394 million and, by the end of the fifty-two week period ending August 27, 1976, were estimated to have increased to approximately $447.6 million.

(15) Totino's brand frozen prepared pizza manufactured and sold by Pillsbury's frozen foods division and frozen prepared pizza manufactured and sold by Fox were, at the time of the acquisition set forth in Paragraph (13b), and had been for some time, in direct and substantial competition.

Relevant Section of the Country

(16) The relevant section of the country is the United States taken as a whole and certain metropolitan marketing areas within the United States.

Market Concentration

(17) Pillsbury and Fox, at the time of agreement and acquisition referenced in Paragraphs (13a) and (13b), and at all times relevant herein were substantial and direct competitors in the manufacture and sale of frozen prepared pizza in the United States as a whole and in a number of major metropolitan marketing areas.

(18) The United States frozen prepared pizza market is highly concentrated with the combined market share of the four largest firms (including Pillsbury) estimated to be in excess of 61%, before Pillsbury's acquisition of Fox, and the combined share of the eight largest firms estimated to be in excess of 84%, before Pillsbury's acquisition of Fox. At the time of the agreement and acquisition referenced in Paragraphs (13a) and (13b) and at all times relevant herein Pillsbury had approximately 14% of the national market while Fox had approximately 2%.

(19) At the time of the agreement and acquisition referenced in Paragraphs (13a) and (13b) and at all times relevant herein Fox and Pillsbury were substantial and direct competitors in the following highly concentrated marketing areas:

a. In the St. Louis marketing area, the four largest firms accounted for more than 78% of all retail frozen prepared pizza sales. Pillsbury was the largest in St. Louis with a market share of 22.13%; Fox was ranked seventh with 4.39%.

b. In the Houston, Texas marketing area the four largest firms accounted for approximately 90% of all retail frozen prepared pizz sales. Pillsbury was the largest in Houston with a market share of 39.0%; Fox was ranked fifth with a market share of 4.57%.

c. In the Charlotte, North Carolina marketing area, the four largest firms accounted for about 75% of all retail frozen prepared pizza sales. Fox was the third largest in that market with a market share of 14.65%; Pillsbury was ranked sixth with a market share of 6.01%.

d. In the Dallas/Ft. Worth marketing area the four largest firms accounted for about 78% of all retail frozen prepared pizza sales. Pillsbury was the largest in that market with a market share of 26.48%; Fox was ranked sixth with a market share of 7.5%.

(20) Fox and Pillsbury at the time of the agreement and acquisition referenced in Paragraphs (13a) and (13b) and at all times relevant herein were also substantial and direct competitors in certain other metropolitan marketing areas.

(21) Concentration in the frozen prepared pizza market has steadily increased over time.

Effects of the Acquisition

(22) The effects of the acquisition set forth in Paragraph (13b) may be substantially to lessen competition or tend to create a monopoly in the relevant markets in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and the acquisition and the agreement antecedent to the acquisition set forth in Paragraph (13a) each constitute an unfair method of competition and an unfair act or practice within the meaning of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), in the following ways among others:

a. the elimination of actual competition between Pillsbury and Fox in the United States frozen prepared pizza market;

b. the elimination of actual competition between Pillsbury and Fox in several major metropolitan marketing areas;

c. increased concentration in the manufacture and sale of frozen pizza in each of the areas described in (a) and (b) above;

d. the encouragement of further acquisitions and mergers by and among the other leading firms in the frozen prepared pizza market.

Violations

(23) The acquisition by Pillsbury of Fox's pizza assets for the asons set forth herein constitutes a violation of Section 7 of the ayton Act, as amended, (15 U.S.C. 18), and Section 5 of the Federal ade Commission Act, as amended, (15 U.S.C. 45).

(24) By entering into the agreement giving rise to the violation described in Paragraph (23), herein, Pillsbury and Fox have violated Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

INITIAL DECISION BY JOSEPH P. DUFRESNE, ADMINISTRATIVE LAW JUDGE

MAY 15, 1978

BACKGROUND

In a complaint dated November 11, 1976, the Commission charged that respondents, The Pillsbury Company and Fox Deluxe Foods, Inc. (Pillsbury and Fox) would violate Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and Section 5(a)(1) of the Federal Trade Commission Act (FTCA) (15 U.S.C. 45) if they consummated an agreement they had made for Pillsbury to acquire Fox. It also was alleged that by entering into the agreement, Pillsbury and Fox had violated FTCA Section 5(a)(1). (Complaint, ¶¶ 1, 23 and 24.) [2]

Section 7, in pertinent part, reads as follows:

> That no corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no corporation subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another corporation engaged also in commerce, where in any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.

Section 5(a)(1) reads as follows:

> Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful.

On November 12, 1976, the day after the complaint originally issued, the United States District Court for the Northern District of Illinois, Eastern Division, in response to complaint counsel's request, issued a Temporary Restraining Order to prohibit consummation of the acquisition. Thereafter, on November 15, 1976, Fox and Pillsbury stipulated to a Preliminary Injunction (No. 76C–4190) which permitted the consummation of the acquisition upon certain conditions.

Pursuant to complaint counsel's motion, the complaint was amended on June 14, 1977, with the acquiescence of Pillsbury's counsel, to reflect that the challenged acquisition had taken place on or about November 15, 1976, and to thus seek divestiture of after-acquired property, relief which was not originally requested. (Amended complaint, ¶ 13B.)

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The printed "First Amended Complaint" is dated June 22, 1977, and contains allegations that:

(a) The manufacture and sale of frozen prepared pizza is a separate, distinct and relevant line of commerce. Frozen prepared pizza is one of the largest and [3] fastest growing of all retail food sales categories. Calendar 1975 national retail frozen prepared pizza sales were estimated at about $394 million and by the end of the fifty-two week period ending August 27, 1976, were estimated to have increased to approximately $447.6 million. (¶ 14.)

(b) "Totino's" brand frozen prepared pizza manufactured and sold by Pillsbury's frozen foods division and frozen prepared pizza manufactured and sold by Fox were, at the time of the acquisition . . . and had been for some time, in direct and substantial competition. (¶ 15.)

(c) The relevant section of the country is the United States taken as a whole and certain metropolitan marketing areas within the United States. (¶ 16.)

(d) The United States frozen prepared pizza market is highly concentrated with the market share of the four largest firms (including Pillsbury) estimated to be in excess of 61%, before Pillsbury's acquisition of Fox and the combined share of the eight largest firms estimated to be in excess of 84%, before Pillsbury's acquisition of Fox. At the time of the agreement and acquisition . . . and at all times relevant . . . Pillsbury had approximately 14% of the national market while Fox had approximately 2%. (¶ 18.)

(e) The adverse effects of the acquisition alleged were:

1. The elimination of actual competition in the frozen prepared pizza market between Pillsbury and Fox in the United States as a whole and in several major metropolitan marketing areas (St. Louis, Mo.; Houston, Texas; Charlotte, N.C. and Dallas/Ft. Worth, Texas); [4]

2. Increased concentration in the manufacture and sale of frozen pizza in each of the areas described . . . above;

3. The encouragement of further acquisitions and mergers by and among the other leading firms in the frozen prepared pizza market. (¶ 22.)

Pillsbury's original Answer dated December 16, 1976, was changed and in lieu thereof, the Answer dated May 26, 1977, was substituted per my "Order Permitting Amendments to Answer," dated June 13, 1976. Fox's Answer was received by the Commission's Secretary on January 11, 1977; however, further consideration thereof is not warranted because complaint counsel advised on April 12, 1977, on the first day of the hearings, that the charges against Fox would not be pressed (Brickfield, Tr. 11-13).

In its Answer, Pillsbury made a general denial of each "allegation, matter, statement or thing" set forth in the complaint, except as otherwise expressly admitted or qualified in the Answer (Answer, ¶1). In addition, several affirmative defenses were asserted as follows:

(1) the complaint failed to state a claim upon which relief may be granted;

(2) the proceeding is not in the public interest;

(3) the acquisition of Fox by Pillsbury violated neither Clayton §7 nor FTCA §5 because Fox was a failing company at all times material to the acquisition;

(4) dismissal of the complaint with attorney's fees, costs and disbursements to Pillsbury, as provided by law, was requested. (Answer, pp. 4-5.)

A separate Answer to the Amended Complaint was not filed (French, Tr. 7). [5]

However, the first two affirmative defenses asserted by Pillsbury were negated by the Preliminary Injunction, entered into by all the parties. It provided that:

1. The complaint stated a claim upon which relief under Section 13(b) of the FTCA might be granted; and that an order would be in the public interest;

2. A new company would be formed by Pillsbury to carry on Fox's frozen prepared pizza business viably, separately and independently so that future divestiture would not be hindered if Pillsbury lost the case;

3. Commission representatives upon written request and reasonable notice could have access to any information relating to matters contained in the Court's Order and would be permitted to interview officers and employees of Pillsbury regarding any such matters;

4. The injunction is to continue in full force and effect until the complaint is dismissed by the Commission, set aside by a court on review or the Commission order has become final;

5. The parties agreed to expedite the administrative proceeding.

Pursuant to the Stipulation and Order, Pillsbury caused a new company, Fox Deluxe Pizza Company (Fox Pizza), to be established to carry on the frozen prepared pizza business of Fox. Pillsbury was also required to cause Fox Pizza to hire adequate personnel; to transfer $1,000,000 to Fox Pizza to be used to acquire manufacturing equipment and improve the Fox facilities; to cause at least 700,000 cases, or one-third of Fox Pizza's total annual production, to be Fox Pizza's own brand; to cause Fox Pizza to reinvest all earnings and pay no dividends; to cause Fox Pizza not to become insolvent; to enter into an Agreement whereby Fox Pizza manufactured pizza for Pillsbury; to use its best efforts to maintain the Fox Pizza brand in the marketplace and to improve the quality of the Fox Pizza product; [6] to refrain from using Fox Pizza's trade secrets or know-how; to notify all brokers selling the Fox Foods brand of pizza that Fox Pizza would continue to market and distribute product independently and in competition with Pillsbury; to refrain from interfering with the independent judgment of Fox Pizza or make any changes other than in the ordinary course of business; and not to permit any deterioration of Fox Pizza which might impair its capacity for the manufacture, distribution or sale of frozen prepared pizza. (Stipulation and Order, November 16, 1976; RPF 14.)

On November 24, 1976, the Commission instructed the administrative law judge to take all appropriate steps to expedite the proceedings and to submit brief, written quarterly reports to it as to the procedural status of the matter and the steps taken to effect expedition. ("Instructions to Administrative Law Judge" dated November 24, 1976.) The last of five such reports was submitted on February 14, 1978.

The case-in-chief was presented in Washington, D.C., on April 12–13, June 14, 20–23, 27–30, July 5–8, 11–14 and September 15, 1977. The case-in-defense was presented in Joplin, Missouri, on October 19–20, in Minneapolis, Minnesota, on October 25–28, and in Washington, D.C. on November 2, 3 and 8–11, 1977. Complaint counsel's case-in-rebuttal was presented in Washington, D.C. on December 7–8 and 13, 1977. Counsel for Pillsbury did not present a case-in-rebuttal after certain stipulations were worked out with complaint counsel, he had reviewed the complete transcript and had offered more evidence. Additional evidence, some offered by each side, was accepted per my Order dated February 13, 1978. The record was closed on February 14, 1978, per my Order dated January 23, 1978.

In total, 43 witnesses testified; 29 for the Commission and 14 for Pillsbury. There are 76 Commission exhibits and 72 Pillsbury exhibits. In accord with Commission Rule 3.43(g) those few exhibits which were rejected have been retained in the official record. There are 3818 pages of transcript of the adjudicative hearings. [7]

Bases for the Findings of Fact; Abbreviations Used

The findings of fact following are based on a review of the allegations made in the complaint, respondents' answers, the documentary evidence, and consideration of the demeanor of the witnesses. In addition, the proposed findings of fact, conclusions and proposed orders, together with reasons and briefs in support thereof filed by each side have been given careful consideration. To the extent not adopted by this decision in the form proposed or in substance, they are rejected.

For convenience, the findings of fact include references to supporting evidentiary items in the record. Such references are intended to serve as guides to the testimony, evidence, and exhibits supporting the findings of fact. They do not necessarily represent complete summaries of the evidence considered in arriving at such findings. The following abbreviations have been used:

Tr.	– Transcript, preceded by the name of the source of the information, followed by the page number.
CX	– Commission's Exhibit, followed by its number.
RX	– Respondents' Exhibit, followed by its number.
CCPF and CCB	– Complaint counsel's Proposed Findings and Brief
RPF and RB	– Respondents' Proposed Findings and Brief.

Findings of Fact

Commission Jurisdiction

1. Pillsbury is engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act (Complaint and Answer, ¶ 8; RPF 5). Section 11 of the Clayton Act authorizes the Commission to enforce compliance with Section 7 of that Act (and other sections as well) with regard to acquisitions by corporations such as Pillsbury [8] (15 U.S.C. 21).

2. To and including November 15, 1976, Fox was engaged in commerce as defined in Section 1 of the Clayton Act. (Complaint and Answer, ¶12; RPF 9.) Being "in commerce," as defined in the Clayton Act also constitutes being "in commerce" under the FTC Act.

The Pillsbury Company

3. Pillsbury is a Delaware corporation with its principal office at the Pillsbury Building, 608 Second Ave. South, Minneapolis, Minnesota (Complaint and Answer, ¶4, RPF 1.)

4. Pillsbury is a manufacturer and marketer of a wide range of food products, including prepared baking mixes, refrigerated dough products, flour and frozen prepared pizza (Complaint and Answer, ¶5; RPF 2.) It also operates restaurant chains (*i.e.,* "Burger King," "Steak and Ale" and "Poppin Fresh Pie Shops") as subsidiaries. (Behnke, Tr. 19.)

5. In its fiscal year ending May 31, 1976, Pillsbury had revenues

in excess of $1.5 billion and net income in excess of $41 million. Pillsbury is among the 200 largest United States corporations. (Complaint and Answer, ¶6; RPF 3.)

6. Pillsbury acquired Totino's Finer Foods, Inc. (Totino's) in November 1975, a manufacturer and seller of frozen prepared pizza. Totino's gross sales for its fiscal year ended October 31, 1975, were approximately $39 million. For the twelve-month period ended October 31, 1976, Totino's gross sales as a Pillsbury subsidiary were approximately $48 million. (Complaint and Answer, ¶7; RPF 4.)

7. Pillsbury projects its profits from 1977 to 1981 to be a 10.6% return on invested capital, which is slightly lower than the average 11% return on investment for all manufacturing industries during the period 1960 to 1970. (Cady, Tr. 3340–41.) **[9]**

Fox Deluxe Foods, Inc.

8. Fox was an Illinois corporation with offices at 222 South Riverside Plaza, Suite 442, Chicago, Illinois. (Complaint and Answer ¶9; RPF 6.)

9. Immediately before its acquisition by Pillsbury on November 15, 1976, Fox was a manufacturer or processor and seller of food products including poultry, butter, eggs and frozen prepared pizza. (Complaint and Answer, ¶ 10; RPF 7.)

10. Fox had net sales of approximately $12.2 million and assets of approximately $3.1 million in its fiscal year ended February 29, 1976. Frozen pizza sales by Fox in that fiscal year were $7.3 million gross, $6.1 million net. (Complaint and Answer, ¶ 11; RPF 8.)

11. Fox was a "price brand" of frozen prepared pizza. The firm relied on the brand's relative low cost and frequent discount promotions, rather than high advertising activity, to attract business. (Francis, Tr. 660–61; DeLapa, Tr. 1206; CCPF 190.)

12. Prior to the acquisition, Fox's ability to obtain and keep geographic distribution varied. Its pizza was sold in a variety of areas in the Midwest and Southwest but did not remain in distribution in smaller areas within these larger ones for long periods. (Nickel, Tr. 493; RPF 112.)

13. As a part of the case-in-defense, there was a tour of the Fox plant in Joplin, Missouri on October 19, 1977 by the administrative law judge and counsel. Testimony was taken (Tr. 2144–2317). The witnesses were Donald E. Balster, Vice President of Operations of Fox Pizza (Balster, Tr. 2144), Rupert Spencer, Maintenance and Engineering Manager of Fox Pizza (Spencer, Tr. 2145), and John Jordan, Quality Assurance Manager of Fox Pizza (Jordan, Tr. 2218–

19). Areas observed and/or described during the tour are identified on floor plans entered in evidence as RX 12, RX 13, and RX 14.

14. Prior to the acquisition, 50 Fox production employees had been laid off. Since the acquisition, employment at the plant has grown from 75 to 180 production personnel and the plant has moved from one shift to two. (Balster, Tr. 2279-80; RPF 221.) **[10]**

15. The parties stipulated that had Dr. R.E. Baird, the U.S.D.A. circuit supervisor having jurisdiction over the Joplin plant testified, he would have said that before the acquisition: (a) the Fox plant was never completely rodent-proofed; (b) the meat room floor was deteriorating rapidly; (c) the cooker in the meat room leaked; (d) the oven in the bakery was difficult to clean and frequently caused fires among the pizza crusts; and (e) peeling paint on the walls of the sauce room and meat room necessitated daily scraping. Dr. Baird also would have said that at the time of the acquisition by Pillsbury, Fox had agreed with him to install a new ceiling in the bakery, correct deficiencies of the floor and walls in the meat room, and rodent-proof all exterior walls; however, it had not accomplished any of these corrections. (CX 76, ¶21; RPF 223.)

16. In mid-1975, there was a meeting between Mr. Joe Fox, chairman of the board of Fox, and Mr. William Bokman, a vice-president of Peavey Company. Mr. Bokman concluded that, although the company was for sale, it was not attractive to Peavey because: (a) Fox's frozen prepared pizza product was in the low-quality, low-price segment of the pizza business, in which Peavey had no interest; (b) there was very little or no management strength in the company; and (c) the new building, as described to him, did not sound like a major asset. (Bokman, Tr. 2597, 2599-2600; RPF 198.)

17. Previously, a Vice-President for Corporate Planning and Business Development of Anderson-Clayton Company, Houston, Texas, a food and food related producer/distributor had looked into the possibility of acquiring Fox. (Glasgow, Tr. 2854.) Mr. Glasgow met Mr. Fox and concluded that, although Fox was for sale, he perceived it as a relatively small company, with small sales, an old plant, a limited geographical area of operation, and a small regional brand at the low-price end of the market with nothing to recommend it to Anderson-Clayton. (Glasgow, Tr. 2858.) Mr. Fox did not recall discussions with anyone other than Peavey, Anderson-Clayton, and Pillsbury. (Fox, CX 46, p. 32; RPF 199.)

18. During the period 1972 to 1975, Fox earned substantial profits. Its sales increased from \$6.4 million to \$11.2 million; its total debt declined from \$1.4 million to \$860,000. The company reportedly had a current structure with working capital of \$900,000 and current

ratio [11] of 2.15. Its net worth increased by over 50% to $1.7 million. However, in December of 1975, the company obtained a loan of $300,000 from Harris Trust and Savings Bank of Chicago, Illinois (Harris) to help finance its new plant at Joplin, Missouri. Harris was aware that the company was using short-term financing to finance long-term assets, but concluded that the proposed loan could be repaid in a year by means of liquidation of Fox's Hotel and Restaurant ("H&R") Division, which had become "a drag on profits" by generating "large losses." (RX 48; RX 49; RPF 179.)

19. In January of 1976, credit analysts at Harris expressed concern over losses by Fox in October and November 1975. (RX 51.)

20. Fox began pizza operations in Joplin on February 16, 1976. (CX 49, p. 1.) On March 22, 1976, production at Joplin was at 50–80% of capacity. On May 17, 1976, in a report to the directors of Fox, it was reported that: (a) sales for the first two months in Joplin were 20% below projections; (b) production efficiency was unfavorable; (c) severe competition, including competitive pricing below the Fox break-even point, was being encountered; and (d) losses at the H&R Division were draining off capital needed in the pizza business. (RX 16; RPF 186.)

21. On March 23, 1976, the Harris employee monitoring the loan, Barbara J. Pite, recommended a 90-day extension of the $300,000 loan. The sale of the H&R Division, which was to have enabled Fox Foods to repay the loan, had not taken place, and the H&R Division was continuing to incur losses. While the overseer of the loan thought that Fox's pizza operation had good earning potential, she told her supervisors that the frozen prepared pizza business "is very competitive and margins are narrow." Extension of the loan was approved, but with recognition of an uncertain operating outlook, the unprofitability of the H&R Division, and possible start-up problems in the company's new plant. (RX 52 and 53; RPF 180.)

22. On May 18, 1976, Ms. Pite recommended an additional $50,000 for Fox Foods from Harris. The operations in Joplin were not going as well as hoped with production costs running too high and margins being squeezed. (RX 54.) This $50,000 additional loan was approved but concern was expressed over Fox's failure to sell the H&R Division. (RX 55; RPF 181.) [12]

23. By May 19, 1976, "excessive downtime" appeared to require a further capital investment in equipment. At the same time more money was needed for co-op (supplier-reseller shared cost) advertising programs. (RX 17.) By June 8, 1976, intense competitive activity, with resulting price wars, appeared likely to force Fox to rely more

on private label as it became more difficult to compete with the major companies. (RX 20; RPF 187.)

24. By June 14, 1976, the chairman of Fox reported to the board of directors that no final offer had yet been received for the H&R Division. (CX 50.) The board also received a report from an outside consultant concerning the Joplin plant indicating that: (a) the economic advantages anticipated in moving to Joplin had not been realized; (b) much of the equipment transferred from Carthage to Joplin presented problems; (c) the baking environment was unsatisfactory and required several modifications; (d) the oven was unsuitable; (e) the topping line and processes were inefficient and wasteful; (f) the conveying system needed to be rearranged; and (g) the packaging machinery was not capable of meeting its goals. "As a minimum" the plant would require $61,820, and this would not include other needed changes, such as "rodent control curbs." (CX 50, pp. 3 & 4; RPF 188.)

25. On July 22, 1976, Ms. Pite asked that the Fox loan be raised by Harris to $500,000 and extended for another 90 days in the expectation that the H&R Division would be sold or liquidated or that all of Fox would be sold. (RX 56; RPF 182.)

26. By this time, Harris was considering a restructuring of the Fox debt that would have given Harris a security interest in Fox's receivables and inventory. (Weisenborn, Tr. 2811.) This would have resulted in an increase in the interest rate charged Fox Foods by Harris. (Weisenborn, Tr. 2843; RPF 183.)

27. By August 3, 1976, the negotiations for sale of the H&R Division had failed by reason of the refusal of the prospective purchaser to enforce collection of Fox's accounts receivable. (CX 51, p. 4.) By this time, Pillsbury had entered the scene with an offer to purchase Fox (CX 51, p. 5) but severe competitive pressures in the marketplace were hampering Fox's operations. Large food [13] corporations were bankrolling the pizza companies and intensifying competition in each market they entered. (RX 21.) The manager of the Joplin plant urged plant investment in excess of $258,000. (RX 15; RPF 189.)

28. That part of operations having to do with Fox's frozen prepared pizza business was profitable in its fiscal year ending February 23, 1976, (Boyce, Tr. 372) as well as during the period from March 1976 until the time of the acquisition in November 1976. (Boyce, Tr. 2395–96.) The Fox frozen prepared pizza business also was profitable in the months of September and October 1976 *(Id.)*; in the month of September alone, Fox showed a profit in the amount of $43,000. (CX 67; CPF 207.)

29. On November 15, 1976, the date on which Pillsbury acquired Fox, it was discovered by Pillsbury that $272,000 in signed but unmailed checks for debts owing to vendors were being held by Fox because of insufficient funds to cover them. (Walker, Tr. 2872–74, 2886; RX 59–63.) Pillsbury advanced $130,000 to cover the checks. (Walker, Tr. 2888.)

30. The causes of Fox's financial decline were: (a) its frozen pizza business was doing well but needed additional capital and (b) its H&R Division was incurring losses and encountering a variety of operating problems. (CX 47, p. 3.) Throughout fiscal 1975, freezer problems at the pizza plant in Carthage, Missouri, resulted in extraordinary expenditures averaging $30,000 per month above normal. (Boyce, Tr. 2408–09.) In addition, higher costs and prices and unusually warm autumn weather in late 1975 reduced pizza sales, with resulting losses in October and November of that year. (CX 48.) At the same time, the decision to transfer Fox's pizza operations to Joplin, Missouri, necessitated the financing at the Harris Trust, discussed above. Fox did have some prospect, in December of 1975, of selling its H&R Division, but only if it were willing to guarantee the accounts receivable. (CX 48, p. 2; RPF 185.)

31. Financial experts testified that:

(a) There was a very substantial deterioration in the company's financial position from 1975 through November of 1976 (Horsch, Tr. 2700);

(b) By November of 1976 the company's current assets-liabilities ratio had fallen to the point where not only [14] did it not have excess cash, but it was in need of substantial money (Horsch, Tr. 2700–01);

(c) Freezer problems at the old plant cost $30,000 per month and the move to the new plant was undertaken without effective long-term financing (Horsch, Tr. 2701);

(d) Start-up costs in Joplin had been underestimated by about $100,000 (*cf.* Boyce, Tr. 2414), and Fox never did inject sufficient capital into the new plant to enable it to produce in an efficient manner (Horsch, Tr. 2701);

(e) The company lacked the management to solve its problems; the chairman of the board was part-time and the president was really a sales manager; a full-time president was lacking. (Horsch, Tr. 2702; *cf.*, Weisenborn, Tr. 2822–23; CX 4, *in camera,* p. 12; Bokman, Tr. 2599–2600; Glasgow, Tr. 2858);

(f) A prompt infusion of new capital approximating $491,000 was urgently required by Fox in the autumn of 1976 (Horsch, Tr. 2705–09);

(g) It was extremely unlikely that such an infusion of capital would come from venture investment and to obtain it from a finance company would have resulted in much higher interest rates for Fox Foods (Horsch, Tr. 2714; Fitzgerald, Tr. 2972–84; RPF 192).

32. Complaint counsel's financial expert, Assistant Professor Peter Jones from the Harvard Business School (Jones, Tr. 3620) limited his testimony to the frozen prepared pizza operations of Fox. He said that the hotel and restaurant business clearly had to be closed or sold and that the future viability of Fox as a company depended on the future viability of the pizza business. (Jones, Tr. 3712.) He added that the H&R Division appeared to represent a drag which would not be acceptable, that his opinion as to Fox's viability turned on Fox's disposing of the H&R Division because "it was just a bad operation steadily for the past few years." (Jones, Tr. 3717–18, 3723–24; RPF 194–5.) **[15]**

33. In anticipation of consummation of the acquisition, Pillsbury caused the Fox cooked-meat room operations to be closed on November 1, 1976, and began to purchase cooked meat from Armour Foods. (RX 41; RPF 229.) After the acquisition, some Fox brand product was destroyed by Pillsbury and processed meat was purchased from another supplier until a new meat processing system could be installed. (Francis, Tr. 651–53; RPF 230.)

The Acquisition

34. On or about October 6, 1976, Pillsbury and Fox agreed that the former should acquire those assets of the latter which were used in the production and sale of frozen prepared pizza ("pizza assets") and on November 3, 1976, Pillsbury and Fox entered into an agreement whereby Pillsbury would acquire the "pizza assets" for $3 million in Pillsbury common stock. (Complaint and Answer, ¶ 13; RPF 10.) Pillsbury made the acquisition as agreed and immediately divested all assets of Fox not used in the manufacture and sale of frozen prepared pizza. (RPF 15.) However, pursuant to the Stipulation and Order issued by the district court, mentioned above, Fox was to be held separate as a corporate entity, *i.e.,* Fox Pizza, and to be operated by separate and independent management in Joplin, Missouri. (RPF 12–13.)

35. Pillsbury acquired Fox in an effort to satisfy short-term production requirements. (CX 2, *in camera,* p. 125; Levin, Tr. 149; Francis, Tr. 624.) Initially, Pillsbury intended to accomplish this

objective by entering into a contract-packing arrangement with Fox, but the food safety problems discovered at Fox eliminated the contract-packing alternative. (Levin, Tr. 224, 226–27; Francis, Tr. 625–26.)

Pizza Described

36. "Pizza" is a food having a bread dough base or crust that is almost always topped with a tomato-based sauce, cheese and may have garnishes such as pepperoni, sausage, mushrooms, anchovies, and the like. (Behnke, Tr. 25; Chamberlin, Tr. 1522; Francia, Tr. 1567; Kuphal, Tr. 2635–36; RPF 16.) [**16**]

37. Pizza is sold with a thick, thin, or a French bread crust. It may be square, oblong or round and may be sold whole or in slices. (RX 6, p. 2; Chamberlin, Tr. 1522–23; Barton, Tr. 1463–64; MacDonald, Tr. 2917; RPF 18.)

38. It may be sold to the consumer frozen, refrigerated, in a dry mix form, in ingredient form–that is, a consumer may purchase separately a grocery shelf-stable crust and make or purchase other ingredients for sauce and topping. (RX 25; RX 25A–25F; RX 27B–36B.) It also may be made from "scratch" at home, may be purchased freshly baked at a restaurant or pizzeria (a restaurant featuring pizza) or may be purchased unbaked or partially baked at a conventional restaurant or at a pizzeria. Pizza also is sold in bars and taverns, schools, grocery stores, military commissaries, delicatessens, vending machines, and other places where food is available for sale. (Behnke, Tr. 93; Caron, Tr. 998–99; Miller, Tr. 949; Follansby, Tr. 1618–19; Dursteen, Tr. 2323–24; Stauffer, Tr. 2107–08; MacDonald, Tr. 2924–25; RPF 19.)

39. Frozen prepared pizza has a shelf life of four to six months, as compared to the shelf life of refrigerated pizza which is five to eight days. (Behnke, Tr. 20–22; Perrin, Tr. 2511–12.)

40. Refrigerated pizza is displayed in the dairy case whereas frozen prepared pizza is displayed in freezer cabinets. (DeLapa, Tr. 1165–66.) There are chemicals which must be put into the dough, the cheese and the sauce to preserve a refrigerated pizza that need not be put into a frozen prepared pizza. (DeLapa, Tr. 1208–09; CCPF 98.)

41. Dry mix pizza has a longer shelf life than frozen prepared pizza. (Roxbury, Tr. 804) The sales trend of dry mix pizza is flat. The sales trend of frozen prepared pizza is up. (Roxbury, Tr. 795; Carpenter, Tr. 1349–50; CCPF 99.) [**17**]

Frozen Prepared Pizza–The Relevant Product Market

42. The manufacture and distribution of frozen prepared pizza in significant quantity is a development of relatively recent origin. For the most part, it is a business which had its beginnings in pizzeria restaurants started by families of predominantly Italian-American background. For example, Totino's, which is now owned by Pillsbury, began as a take-out pizzeria in 1952. In 1962 the Totinos decided to market frozen pizza at retail. (CX 10, p. 1.) Similarly, Saluto Foods, now owned by General Mills, began as a pizzeria in 1963. (DeLapa, Tr. 1073; CX 3, p. 3.) The "Tree Tavern" brand of pizza derives its name and origin (19 or 20 years ago) from the Tree Tavern restaurant in Paterson, New Jersey. (Francia, Tr. 1538–40.)

43. When they opened shop, frozen pizza manufacturers usually were small, local or regional businesses requiring little capital. This, because the manufacturing and distribution processes were relatively simple. (DeLapa, Tr. 1073–74; Francia, Tr. 1539–40; Pizza, Tr. 743–44.) Competition was not strong so these small companies were able to expand into many trade areas that would be difficult for them to enter today. (DeLapa, Tr. 1089; Pizza, Tr. 714; Caron, Tr. 1033; RPF 235.)

44. Frozen prepared pizza is produced by mixing dough and, by the pressed or sheeted method, reducing the thickness of the dough and cutting it into predetermined shapes of a specific size. If a sheeted method is employed, the crusts are "proofed," *i.e.*, placed in a piece of equipment where the temperature and humidity can be controlled for a long enough time to allow the product to rise. Crusts are then baked in an oven and transported on a conveyor belt to a topping area where sauce, cheese and other toppings are applied manually or automatically. The pizza is then frozen in a blast freezer (quick freezer) and packaged manually or automatically. (Behnke, Tr. 25–26; Francis, Tr. 609–12; Kuphal, Tr. 2645; CCPF 81.)

45. Most frozen prepared pizza contains no special ingredients differing from other forms of pizza. While each manufacturer may feel that his special blend imparts a special taste to his product, the ingredients of all forms of pizza are about the same. (DeLapa, Tr. 1074; Selby, Tr. 1247–50, 1258–59; RPF 46.) [18]

46. There is nothing in the manufacture and distribution of frozen prepared pizza which makes it an unusual food product. It is manufactured and then sold by food brokers who represent the manufacturers. Purchasers at this, the supply side of distribution, are wholesalers and chain grocery retailers. On the retailing side, wholesalers sell the product to resellers who, in competition with the

chain retailers, sell the pizza to the consuming public. (Patterson, Tr. 1739; RPF 80.)

47. Separate buying offices of the same retail food chain or the same voluntary wholesalers are viewed as separate and distinct customers. (Boyce, Tr. 366–67; Carlson, Tr. 560–61.) For example, among Fox's top ten customers are three different divisions of Winn-Dixie Stores, Inc., a retail food chain (CX 16); and among Totino's top ten customers are two different buying offices of Super-Valu Stores, a wholesaler, and two different buying offices of Safeway Stores, Inc., a retail food chain. (CX 26 *in camera;* CCPF 137.)

48. Food brokers typically represent a variety of manufacturers–"principals"–handling a large number of frozen and non-frozen food and non-food products in a single primary geographical area of responsibility. (Walling, Tr. 1321–22; Patterson, Tr. 1758–59; Carlson, Tr. 508–09; RPF 91.)

49. The boundaries of a broker's area of primary responsibility will vary according to the size of the broker organization and changing business conditions. (Walling, Tr. 1328–29; Patterson, Tr. 1754–55; Carlson, Tr. 570; Nickel, Tr. 451; Pizza, Tr. 738; Rosen, Tr. 1885; RX 1; Walling, Tr. 1312; Mosley, Tr. 1816–17; RPF 92.)

50. The process of preparing a frozen prepared pizza generally involves different methodologies and machinery than the process of making a pizzeria pizza. (DeLapa, Tr. 1074; Selby, Tr. 1232–36) Pizzeria pizzas generally are not frozen before sale to the customer and do not contain preservatives often found in frozen prepared pizzas. (Selby, Tr. 1235–36; CCPF 82.) **[19]**

51. Frozen prepared pizza can be manufactured on a large scale basis. When this is done, some of the machinery utilized may be customized. (Dursteen, Tr. 2331–32) Most of the machinery used in the manufacturing process is similar to machinery used to manufacture other baked goods or frozen foods. The equipment used to mix the dough, roll it out and bake it, is similar to equipment used in the mass manufacture of other baked goods. The conveying system within the factory appears to be standard. (*See* Finding 144 re plant tour). The blast freezer is typical of those used in the manufacture of any food which must be fast-frozen. (Kuphal, Tr. 2634–58; RX 58.)

52. Frozen prepared pizza can be manufactured in the kitchen of a restaurant and one witness began in a garage. (DeLapa, Tr. 1073; Francia, Tr. 1539–40) Frozen prepared pizza can be easily assembled by a few employees and frozen. (Stauffer, Tr. 2112–13.)

53. In the late 1960's, large conglomerate food companies began to enter the frozen prepared pizza market, usually by acquisition, changing the nature of competition within the frozen prepared pizza

industry. (Pizza, Tr. 714, 766; Malkowicz, Tr. 858; DeLapa, Tr. 1075, 1079–81; Francia, Tr. 1557; CCPF 25; CCPF 156.)

54. There is a trade association, the National Frozen Pizza Institute, to which many manufacturers of frozen prepared pizza belong. Pillsbury is a member. (Boyce, Tr. 383; Francis, Tr. 612; Pizza, Tr. 699; Malkowicz, Tr. 879; DeLapa, Tr. 1090.) The Institute is open primarily to domestic manufacturers of frozen prepared pizza but associate membership is available to others having an interest in the frozen pizza industry. (Pizza, Tr. 700; CCPF 26.)

55. Many manufacturers, whether they are independent firms or separate divisions of larger firms which produce frozen prepared pizza, do not produce other types of pizza. (CCPF 27 and 87.) For example:

a. Frozen Foods Division of Pillsbury (separate division producing only frozen pizza). (Francis, Tr. 608; Nickel, Tr. 402–03.) [20]

b. Fox (produces only frozen pizza). (Boyce, Tr. 341–42.)

c. Anthony J. Pizza Inc. (produces only frozen pizza). (Pizza, Tr. 679.)

d. Saluto Foods Corp. (separate division of General Mills producing only frozen pizza). (DeLapa, Tr. 1072.)

e. Ellio's Pizza (separate division of Purex producing only frozen pizza). (Malkowicz, Tr. 857, 885.)

f. Stouffer's Frozen Foods (produces only frozen pizza). (Stauffer, Tr. 2114.)

56. Plants producing frozen prepared pizza containing meat are U.S.D.A. inspected and subject to U.S.D.A. guidelines and regulations. (Francis, Tr. 627–28; DeLapa, Tr. 1148–51; Balster, Tr. 2202–03; CCPF 90.)

57. Frozen prepared pizza is a food product which must be kept frozen to avoid deterioration and must be stored and transported in a controlled temperature. (Caron, Tr. 1008–09; Perrin, Tr. 2534–36; CCPF 92.)

58. Manufacturers and brokers of frozen prepared pizza regularly "cut" (*i.e.,* have a taste test, usually for a reselling buyer) against competing brands of frozen prepared pizza. (Pizza, Tr. 701–02; Malkowicz, Tr. 883–84.) They rarely cut against any other products. (Pizza, Tr. 701–02; Malkowicz, Tr. 883–84; CCPF 29.)

59. Pillsbury "cuts" much more often against other brands of frozen prepared pizza than against dry mix, refrigerated or pizzeria pizza. (Behnke, Tr. 35–37; CCPF 30.)

60. Brokers of frozen prepared pizza cut against competing

brands of frozen prepared pizza but do not cut against dry mix, refrigerated or pizzeria pizza. (Moore, Tr. 1795–96; CCPF 31.)

61. Manufacturers of frozen prepared pizza regularly monitor the competitive activities of other manufacturers of frozen prepared pizza and do not regularly monitor the competitive activities of manufacturers of other products. (Boyce, Tr. 375–76; Pizza, Tr. 703–04; Carlson, Tr. 515–17, 530, 558–59; Malkowicz, Tr. 883; DeLapa, Tr. 1098–99; Carpenter, Tr. 1334–35; Barton, Tr. 1406–07; Chamberlin, Tr. 1480–81; Francia, Tr. 1548–49; Dursteen, Tr. 2332–33; CCPF 33–34.) [21]

62. Brokers do not report on the competitive activity of manufacturers of other products to manufacturers of frozen prepared pizza. (Carlson, Tr. 530; Walling, Tr. 1301; Patterson, Tr. 1748–49; Mosley, Tr. 1830–31; CCPF 35.)

63. Consumers view pizzeria pizza as a more desirable product than frozen prepared pizza. (Dursteen, Tr. 2346–47; Rowlatt-Smith, Tr. 3794–95; CCPF 76.)

64. They do not readily substitute other forms of pizza for frozen prepared pizza and are more likely to choose hamburgers, frankfurters or ingredients for salads as alternatives to frozen prepared pizza than refrigerated, dry mix or pizzeria pizza. (RX 64F; Neadle, Tr. 3125–26; Cady, Tr. 3407–08; CCPF 75.)

65. Manufacturers of frozen prepared pizza view pizzeria pizza as the "golden standard." (Nickel, Tr. 479–80; Chamberlin, Tr. 1516.) Generally they feel that frozen prepared pizza is of a lesser quality than pizzeria pizza. (DeLapa, Tr. 1106–07; Dursteen, Tr. 2346–48; Paulucci, Tr. 2424; CCPF 100.)

66. Most manufacturers of frozen prepared pizza view all food as competing for the consumer's food dollar, but see frozen prepared pizza as a distinct market and the primary source of their competition. (Pizza, Tr. 696–97; Roxbury, Tr. 842–43; DeLapa, Tr. 1098–99; Rowlatt-Smith, Tr. 3735–36; CCPF 44.)

67. Manufacturer-witnesses who listed specific competitors listed only other frozen prepared pizza manufacturers. (Pizza, Tr. 694–95; Roxbury, Tr. 821; Francia, Tr. 1550.) They did not look upon manufacturers of refrigerated pizza, dry mix pizza or pizzeria pizza as direct competitors. (DeLapa, Tr. 1098–99; Pizza, Tr. 695–96, 806; Carpenter, Tr. 1365–68; Francia, Tr. 1549; Barton, Tr. 1406; Stauffer, Tr. 2119; Paulucci, Tr. 2424; CCPF 46–49.)

68. In their pricing decisions, manufacturers of frozen prepared pizza consider the prices set by other manufacturers of frozen prepared pizza. (Boyce, Tr. 375–76; Francia, Tr. 643–44; Roxbury, Tr. 786–87; Malkowicz, Tr. 861; CCPF 192.) They do not take into account

the prices set by manufacturers of dry mix, refrigerated, pizzeria or institutional pizza in establishing their prices. (Roxbury, Tr. 794–95; Malkowicz, Tr. 861; Caron, Tr. 1008; CCPF 35, 37, 66–67, 104, 111.) [22]

69. Manufacturers of frozen prepared pizza regularly receive only data concerning frozen prepared pizza. (Francis, 621–22; CCPF 38.)

70. It is considered a conflict of interest for brokers to handle two manufacturers' frozen prepared pizzas at the same time. (Pizza, Tr. 704–05; DeLapa, Tr. 1117–18; Walling, Tr. 1290; Patterson, Tr. 1781–82.) The manufacturer of "John's" brand testified that he had lost brokers because of such conflicts. (Pizza, Tr. 707; CCPF 41.)

71. In its 1976 Annual Report, Pillsbury refers to "national retail frozen pizza sales." (CX 1, pp. 8–10; Francis, Tr. 616, 618; CCPF 61.)

72. Pillsbury views itself as competing against other manufacturers of frozen prepared pizza. Officials and documents of that company state that the major competitors of Totino's pizza are Celeste, Saluto, Jeno's, Tony's, Chef Boyardee and John's. (Francis, Tr. 639–40; CCPF 64.)

73. Brokers view other brands of frozen prepared pizza as the competition for the frozen prepared pizza which they handle. (Walling, Tr. 1277–79; Patterson, Tr. 1739–40; Mosley, Tr. 1817–19; CCPF 68.)

74. Retailers consider frozen prepared pizza as a separate product category, distinct from other product categories, such as frozen entrees or frozen orange juice. (Bahl, Tr. 289–90; Coles, Tr. 1587–89; Smith, Tr. 1639; Moore, Tr. 1797–99; Urbanowicz, Tr. 1854; CCPF 70.)

75. Frozen prepared pizza is evaluated in terms of movement or retail sales and profitability separately from any other category of product. (Bahl, Tr. 306; Coles, Tr. 1587–89; Smith, Tr. 1639–40; Moore, Tr. 1797–99; Urbanowicz, Tr. 1854; CCPF 71.) [23]

76. Case movement or rate of retail sales of frozen prepared pizza is not compared to case movement of dry mix or refrigerated pizza. (Coles, Tr. 1588–89; Moore, Tr. 1796–99; Urbanowicz, Tr. 1854; CCPF 72.)

77. Position and number of rows or "facings" (*i.e.*, the stack of any product in a retailer's freezer cabinet so that the top package faces the consumer) is of great importance to the sale of frozen prepared pizza. (Bahl, Tr. 293; Caron, Tr. 1003–05; DeLapa, Tr. 1110–12; Patterson, Tr. 1772–75.) Manufacturers of frozen prepared pizza compete against one another for position and number of facings in the frozen prepared pizza section of the freezer cabinet. (Caron, Tr. 1003–05; DeLapa, Tr. 1110–12; CCPF 94.)

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78. Heavy consumer oriented promotion and advertising are required to secure and retain adequate space in retailers' freezer cabinets. (Caron, Tr. 1003–04; DeLapa, Tr. 1084–85; Francia, Tr. 1558–59.) Frozen prepared pizza is in the top 10 to 12 percent of the frozen food products most heavily promoted. (Bahl, Tr. 295–96; CCPF 95.)

Statistical Reports Frozen Pizza Manufacturers Use

79. Manufacturers of frozen prepared pizza rely on reports published by Selling Areas Marketing, Inc., a subsidiary of Time, Inc. ("SAMI") for information on warehouse movement of frozen prepared pizza sold to food stores in defined areas of the United States. (Boyce, Tr. 361; Nickel, Tr. 405–11; Francis, Tr. 621–22; Pizza, Tr. 689; Malkowicz, Tr. 863; Miller, Tr. 951; DeLapa, Tr. 1115–16; Carpenter, Tr. 1333; Chamberlin, Tr. 1473–74; CX 54, p. 1; RPF 99.)

80. SAMI statistics are used for a wide variety of purposes. They are used "in evaluations of how the market quota is progressing" (Barton, Tr. 1395), "to mark the trends in the industry" (Nickel, Tr. 429; Francis, Tr. 621), "as a barometer of how well our broker is doing" (Nickel, Tr. 429); *see also* Chamberlin, Tr. 1474), "as a guide and cross reference to check our own information" (Moore, Tr. 1812), to mark "trends and directions," (MacDonald, Tr, 2951), and where deemed "useful for sales" (Chamberlin, Tr. 1477; RPF 135). [24]

81. Users rely on the SAMI data despite the fact that it is acknowledged not to include at least one of the largest frozen prepared pizza manufacturers (Schwan's) and possibly two (Tombstone) because they do not furnish SAMI with product movement data. (DeLapa, Tr. 1121; RPF 136.)

82. Mr. Chamberlin, Vice President, General Manager, frozen food operation of Quaker Oats (Celeste brand) testified that SAMI is the most practical and acceptable tool available to marketers to monitor market performance because it comes out quickly and can keep management relatively current. This, combined with the experience of management in the field, can provide a reasonably accurate picture of the marketplace. (Chamberlin, Tr. 1519–20; RPF 137.)

83. SAMI is a recognized market survey firm and reports on frozen prepared pizza as a distinct product category in various areas of the United States. (CX 54, p. 2; RX 11, Exhibit A, p. 2; CCPF 79.) When the acquisition occurred, 36 such areas were covered and in 1977, SAMI added three additional local areas to its system for a total of 39. (*See* RX 68.)

84. No witness from SAMI testified; however two stipulations

(CX 54 and RX 11), prepared in consultation with SAMI personnel, and which describe the preparation of SAMI reports, are in the record.

85. SAMI monitors (counts) warehouse withdrawals in areas estimated to encompass 75% of national grocery store sales (CX 54, ¶ 4; RX 11, ¶ 2) and, within those areas, it obtains warehouse withdrawal reports covering, on the average, about 80% of the included grocery products passing through grocery warehouses. (CX 54, ¶ 4; RX 11, ¶ 3; RPF 124.)

86. SAMI cannot statistically predict product movement patterns in other warehouses. (RX 11, ¶ 5.) Patterns of stocking and withdrawals may differ between warehouses which report to SAMI and warehouses which do not. (Kuehn, Tr. 3150; Douglas, Tr. 3455–3457; RPF 124.) [25]

87. SAMI is similarly unable to make a statistically verifiable prediction as to product movement in areas where it does not count movement. "SAMI does not know whether product movement patterns outside its reporting areas are the same as those inside those areas, or that patterns for unreported product movement within an area are the same as those for reported product movement in the same area." (Kuehn, Tr. 3151–56; RX 11, ¶ 14; RPF 124.)

88. Although SAMI counts the movement of private label products, it does not report such movement if there are less than three private label products within a reporting classification in a given reporting area. (RX 11, ¶ 4; RPF 124.)

89. SAMI relies in part on the reporting warehouses to filter out of their reports the products shipped outside defined reporting areas, but SAMI cannot assure that this is always done and SAMI does not insist on the filtering process if such outshipments amount to less than 10% of the total. (RX 11, ¶ 9; *see also* CX 54, ¶¶ 17–19; Kuehn, Tr. 3173, 3175–76; RPF 124.)

90. SAMI uses the same reporting areas to monitor the movement of numerous products (food and non-food, frozen and non-frozen), but this does not reflect any deliberative judgment by SAMI as to what the economic or geographic markets are for any product on which SAMI reports. No attempt has been made by SAMI to relate its reporting areas to food manufacturers' patterns of distribution. SAMI is not aware as to whether such patterns exist. Warehouses reporting to SAMI may ship to stores (a) within a single SAMI reporting area, or (b) within and outside such areas, or (c) into several such areas, or (d) a combination of "(b)" and "(c)" above. Some warehouses reporting to SAMI reportedly ship as much as 40% of their product outside SAMI reporting areas. Warehouses outside

SAMI marketing areas may also ship products into such areas. (RX 11, p. 5; RPF 100.)

91. SAMI developed fixed geographic boundaries for these local areas in order to provide reports that would be consistent over time. (CX 54, ¶ 14.) These boundaries were decided upon after SAMI personnel consulted with the local grocery trade in each area (CX 54, ¶ 12), often using in their consultation, markets defined by the trade publication "Progressive Grocer." (CX 54, ¶ 26; Nickel, Tr. 450–51.) **[26]**

92. SAMI also consulted with the trade in order to insure that the boundaries are not too narrowly drawn (CX 54, ¶¶ 14, 15); but not every local grocery distribution market is covered by the SAMI system (*see* CX 27, p. 10716; Caron, Tr. 1045; Carpenter, Tr. 1334, 1336). SAMI's local grocery distribution areas were designed to encompass the common business operations core of local grocery retailers as well as the wholesalers and the stores they supply. (CX 54, ¶ 14; CCPF 131.)

93. SAMI local marketing areas therefore serve as "rough approximations" of local grocery distribution markets. (Maps of the SAMI areas where Pillsbury's Totino's brand and Fox competed, are found as CX's 37–45.) SAMI areas are similar to broker territories. (Barton, Tr. 1395–96; CCPF 133.)

94. SAMI has developed its local market areas knowing that it would not be possible to cover all of the retail stores served by its participating food operators (the retail chain warehouse and wholesale grocery warehouse operators who submit their warehouse withdrawal data to SAMI). (CX 54, ¶ 3.) The resulting boundaries describe local grocery distribution areas that track warehouse distribution patterns as closely as possible using county lines as boundaries. (CX 54, ¶ 12; CCPF 130.)

95. Manufacturers of frozen prepared pizza rely on SAMI data to describe and analyze local grocery distribution/marketing conditions by brand name. (CX 17A, pp. 11110–11; CX 27 p. 10716; Boyce, Tr. 361–62; Nickel, Tr. 427–28, 432, 437, 439; Carlson, Tr. 510–11, 521–22, 530, Pizza, Tr. 689; Malkowicz, Tr. 864–65; DeLapa, Tr. 1185; Barton, Tr. 1394–96.)

96. Manufacturers often supply SAMI reports on frozen prepared pizza to brokers for use as selling tools to convince buyers for resellers that they should stock more of a particular brand. (Walling, Tr. 1293; Patterson, Tr. 1740; Rosen, Tr. 1882; CCPF 36.)

97. Pillsbury does not regularly subscribe for SAMI reports on products other than frozen prepared pizza except for one summary of

numerous grocery items. (Boyce, Tr. 363; Nickel, Tr. 429–30; Francis, Tr. 621–22; CCPF 37.) [27]

98. Two other market survey firms, Market Research Corporation of America ("MRCA") and A.C. Nielson, also report on sales of frozen prepared pizza as a distinct category of food product. (CX 69; Francis, Tr. 622; Roxbury, Tr. 803; CCPF 80.)

99. MRCA is a consumer diary panel data source. (Kuehn, Tr. 3246–47.) MRCA data are based on a random sample of consumers who fill out diaries each week indicating what products have been purchased by each member in a household. (*See, e.g.,* CX 69.) Such a diary includes product which is distributed by means of direct store delivery, as well as product which is distributed directly to the consumer. (Kuehn, Tr. 3191.) However, Dr. Kuehn testified that MRCA data also contained error. (Kuehn, Tr. 3242, 3260; RPF 141–42.)

100. According to CX 55 *(in camera)* ("SAMI Frozen Brand Shares of All Flavors — U.S. Total, Units: Dollars"), CX 60 *(in camera)* ("SAMI 20 Frozen Pizza Brand Shares of All Flavors — Total U.S., Units: Dollars") and CX 64 *(in camera)*("MRCA" Frozen Pizza Brand Shares of All Flavors — U.S. Total — 1974 through 1976, $(000's)"), the shares of frozen pizza sales in the United States held by various manufacturers were as follows:

CX 55

		1976	1975	1974
Jeno's	-	22.40%	21.65%	16.54%
Totino's	-	18.28%	17.07%	15.07%
Celeste	-	12.69%	12.65%	13.82%
John's	-	8.63%	8.83%	10.05%
Top Four	-	62%	60.20%	55.48%

CX 60

		1976	1975
Jeno's	-	18.82%	17.41%
Tony's	-	15.96%	19.58%
Totino's	-	15.36%	13.72%
Celeste	-	10.66%	10.17%
Top Four	-	60.80%	60.88%

[28] CX 64

		1976	1975	1974
Jeno's	-	15.7%	14.5%	11.0% (Totino's)
Totino's	-	13.7%	13.0%	10.7% (Jeno's)
Tony's	-	11.7%	13.0%	10.4%
Celeste	-	8.2%	7.0%	7.6% (Chef Boyardee)
Top Four	-	49.3%	47.5%	39.7%

Competition in the Frozen Prepared Pizza Industry

101. The evidence concerning (a) the size of the "frozen prepared pizza" market and (b) the shares of this line of commerce held by the major manufacturers is contained in CX 35 and 36. These were prepared by Schwan's Sales Enterprises, Inc., by combining information concerning Schwan's sales of "Tony's" pizza with data obtained from reports prepared by SAMI (Miller, Tr. 951-52); and CX 55-65, which were prepared by complaint counsel on the basis of data drawn from CX 35, CX 36 and certain reports prepared by SAMI and several other firms. (*See* ALJ's Order of October 4, 1977.)

102. In 1975, the year before Pillsbury acquired Fox, the retail frozen prepared pizza industry had sales of $407 million. In 1976, the year the acquisition took place, the national frozen prepared pizza industry had sales of $463 million. Sixteen percent of total national frozen prepared pizza sales occurred in nine of the local markets where Fox and Totino's competed prior to the acquisition in both 1975 and 1976. (CX 36 *in camera;* CCPF 150-52.) [29]

103. In 1976, the year in which the acquisition took place, Pillsbury's Totino's brand ranked third in the national retail frozen prepared pizza industry with 15.4% of sales and Fox ranked eleventh with 1.7% of sales. The acquisition of Fox raised Pillsbury to a 17.1% share of the market. (CX 36 *in camera;* CCPF 178.) The Pillsbury 1976 Annual Report states that Totino's ranked *second* in national market share in both dollars and unit volume. (CX 1, p. 10; CCPF 182.)

104. In 1975, the last full pre-acquisition year, Pillsbury's Totino's brand ranked third in the national frozen food prepared pizza industry with 13.7% of sales and Fox ranked ninth with 2.4% of sales. Thus, Fox and Pillsbury combined had a 16.1% share of the market. (CX 36 *in camera;* CCPF 179.)

105. The acquisition increased the national level of four firm concentration in 1975 market shares from 60.88% to 63.23% and eight firm concentration from 83.49% to 85.84% and increased the national level of four firm concentration in 1976 from 60.80% to 62.53% and eight firm concentration from 83.79% to 85.52%. (CX 36 *in camera;* CCPF 183-84.)

106. Industry leaders' market shares show this trend:

	Top 2 Firms %	Top 3 Firms %	Top 7 Firms %
1973	27.18	39.65	70.74
1974	31.61	45.43	73.51
1975	38.72	51.37	79.50
1976	40.68	53.37	80.74

(CX 55 *in camera;* CCPF 157.)

107. The trend toward concentration probably will continue. Pillsbury's Vice President of Mergers and Acquisitions projected that the top three companies in the frozen prepared pizza industry will capture 60–70% of the national market by 1980. (Levin, Tr. 175.) The Chairman of the Board of Jeno's, Mr. Jeno Paulucci, said that if the present intensely competitive activity of the large companies in the frozen prepared pizza industry continues he believes that the industry will consist of only four or five companies. (Paulucci, Tr. 2431–32; CCPF 159.) [30]

108. The Fox acquisition may trigger the acquisition of other frozen pizza companies. It caused Jeno's to consider purchasing other frozen pizza companies, although such a course of action has been postponed by the company pending the outcome of instant litigation. (Barton, Tr. 1401–02, 1432–34; CCPF 200.) The acquisition by Pillsbury of Totino's triggered the sale of Saluto Pizza to General Mills. (DeLapa, Tr. 1200–02; CCPF 201.)

109. Fox was considered by some other manufacturers of retail frozen prepared pizza, including Saluto and Jeno's, to be among their substantial competitors in a number of local markets. (DeLapa, Tr. 1159–60; Barton, Tr. 1461–62; CCPF 204.)

110. Witnesses from all levels of the distribution chain testified that competition in the frozen prepared pizza industry is extremely "tough." (Levin, Tr. 240, 242–43, 238–39; Caron, Tr. 1030; Patterson, Tr. 1766; Moore, Tr. 1812; Dursteen, Tr. 2330; DeLapa, Tr. 1162, 1223; Malkowicz, Tr. 860, 894–95; Urbanowicz, Tr. 1857; RPF 154.)

111. Many factors have radically altered the nature of the industry in recent years. For example:

(a) Applicable government regulations have become more stringent, thereby increasing the difficulty and expense of entering the business. (Francia, Tr. 1556–58; DeLapa, Tr. 1148–55.)

(b) Although it remains possible to enter the business inexpensively, sustained and significant participation now requires high technology. (Pizza, Tr. 748, 766.) The industry is changing from labor intensive to capital intensive. (Caron, Tr. 1018, 1031–32.)

(c) The entry of large national firms (*e.g.*, General Mills, Purex, Quaker Oats, Pillsbury) has made the business intensely competitive with very heavy advertising and promotional activity. (Pizza, Tr. 704; Bard, Tr. 1721-24; DeLapa, Tr. 1084, 1162; Caron, Tr. 1033-34; Rosen, Tr. 1887-88.) [31]

An exchange between complaint counsel and a witness he called, Thomas Caron of Schwan's Sales Enterprises, the maker of "Tony's" pizza, discloses industry changes:

BY MR. BRICKFIELD:

Q. In response to Mr. French's question about the competition being stronger, you stated they were different competitively, and can you tell us what you mean by that?

A. They are different competitors. The competitors that existed not much more than three years ago — they are basically the people that started in the business. And in the process of the last three years, the competitors have changed from individuals with relatively limited resources to being very large companies in the food business, traditionally with considerably more resources. (Caron, Tr. 1051.)

(d) Coupled with these trends is a widespread tendency of major food chains and distributors to replace lower priced pizzas (such as Fox, Lambrecht, G&W and John's) with private-label products of their own. (RX 22; RPF 236.) The implications of this change for a small underfinanced firm like Fox are clear. If small firms are going to have to support their product with extensive promotions and advertising, it gets more difficult to sustain a reasonable profit a small firm can live with; as a result, small frozen pizza manufacturers will disappear. (Rosen, Tr. 1898-99; Francia, Tr. 1557; DeLapa, Tr. 1193; Paulucci, Tr. 2431-32; Chamberlin, Tr. 1513, 1523, 1524, 1532; RPF 239.)

112. As for future trends, as the larger firms expand nationally (Caron, Tr. 1056; Barton, Tr. 1412; Chamberlin, Tr. 1029, 1500-01; Rosen, Tr. 1896-97) and compete for the available retail space (Chamberlin, Tr. 1518; Pizza, Tr. 770; Francia, Tr. 1562-64), small local and regional firms will find it increasingly difficult to enter the business successfully (Chamberlin, Tr. 1525) many such firms will find it increasingly difficult to keep pace and probably will fall by the wayside. (Chamberlin, Tr. 1523-24, 1531-32; Francia, Tr. 1556, 1564-65.) Even large, national firms will choose to exit from the business in search of more profitable business opportunities because frozen pizza is a very low profit margin business, both for Pillsbury

[32] (*see* Prof. Siegfried's profit comparisons, Tr. 2073-77) and for others as well. (DeLapa, Tr. 1223; Dursteen, Tr. 2330; RPF 237.)

113. These changes/trends, however, have not diminished competition. As witness Mr. DeLapa put it, "There are fewer smaller manufacturers, Your Honor, but there are more larger manufacturers because the category has grown so substantially it has now attracted the capital of the multinational companies." (DeLapa, Tr. 1195.) Among the successful recent entrants are such firms as Campbell ("Swanson's"), Heinz ("LaPizzeria"), Banquet, General Host, and Stouffer's. (DeLapa, Tr. 1141-43; Barton, Tr. 1453-54.) The industry now includes among its number many firms having the financial, technical, and marketing skills to survive and prosper, including General Mills (Saluto), RCA ("Banquet"), Beatrice, Campbell, Heinz (LaPizzeria), Stouffer, Quaker Oats ("Celeste"), American Home Products ("Chef Boyardee"), Jeno's, Fairmont Foods ("Creative Crust") Pillsbury ("Totino's" and "Fox") and Purex ("Ellio's"). (Pizza, Tr. 748-50; DeLapa, Tr. 1146-47; Barton, Tr. 1449-51; Rosen, Tr. 1896-97; RPF 238.)

114. Several large firms have entered into the frozen prepared pizza industry in recent years by acquisition. In addition to the entry of Pillsbury in 1975 by acquisition of Totino's, General Mills entered in 1976 by acquiring Saluto (DeLapa, Tr. 1075), Purex entered in 1971 by acquiring Ellio's (Malkowicz, Tr. 858), and Quaker Oats entered in 1969 by its acquisition of Celeste (Chamberlin, Tr. 1472). In addition, other large and well-financed companies have entered by development and marketing of their own product. These include, Pet, Inc., with a product called El Paso Mexican Pizza (Moore, Tr. 1811), Ore-Ida (Heinz) with a product called LaPizzeria (Rowlatt-Smith, Tr. 3732-33). (Note: Heinz also acquired a frozen prepared pizza manufacturer (Baltino) in 1977 (Rowlatt-Smith, Tr. 3748).) In addition, Fairmont Foods entered with a product called Creative Crust (*see* Dursteen, Tr. 2324-25), and Stouffer did so with its French bread style frozen pizza. (MacDonald, Tr. 2920-24; CCPF 156; RPF 168.)

115. There are strong competitors in every area of the country, and there are different sales leaders in each region and local area. (Caron, Tr. 1045; Pizza, Tr. 715; Francia, Tr. 1550; Barton, Tr. 1410; Malkowicz, Tr. 886.) For example, in St. Louis, one of the submarkets alleged in the complaint, there are many different brands of frozen prepared pizza sold and no one brand dominates. (Pizza, Tr. 761; Smith, Tr. 1630; RPF 155.) [33]

116. The intense competition affects sales and distribution of the larger manufacturers as well as of the smaller ones. Large compa-

nies, such as American Home Products (Chef Boyardee brand) and General Mills (Saluto brand) have lost market share in areas while smaller competitors such as Stouffer's Frozen Foods, and Tree Tavern, Inc., have been able to stay in business and to expand if desired. (Roxbury, Tr. 802; DeLapa, Tr. 1087; Stauffer, Tr. 2112; Francia, Tr. 1550; RPF 156.)

117. In determining the price of their product, manufacturers take into account prices of other brands of frozen prepared pizza. They do not significantly consider the prices of other frozen foods. (*See e.g.,* Rowlatt-Smith, Tr. 3762–63.) Manufacturers promote their product against and in response to promotions of frozen prepared pizza by other manufacturers. (*See* Caron, Tr. 1006–08; RPF 60.)

118. Manufacturer-sponsored sales promotions are offered to retailers at different times in different areas and can be limited to one metropolitan area or to a larger region. (Nickel, Tr. 439–40, 498; Roxbury, Tr. 805; Barton, Tr. 1391–92, 1445–46; RPF 108.)

119. Another form of competition in the frozen pizza industry is found in the attempts of suppliers to get more space for their brand in the pizza section of frozen food cases in retail grocery stores. (Francis, Tr. 662–63; Pizza, Tr. 704–05, 707–08; Roxbury, Tr. 809–10; Malkowicz, Tr. 894–95; Caron, Tr. 1003–05; Chamberlin, Tr. 1517–19; CCPF 138.)

120. Manufacturers examine and evaluate competitive conditions (*e.g.,* pricing and promotional allowances) in each local market separately. (Pizza, Tr. 701; CCPF 141.) Local market knowledge is necessary for manufacturers because retail frozen prepared pizza is a very "market particular" product in that customers and the trade in different markets have vastly differing size and flavor preferences. (Carlson, Tr. 575–78; Pizza, Tr. 711–12; Malkowicz, Tr. 879; Chamberlin, Tr. 1479–80.) Pittsburgh is a "cheese" market (Carlson, Tr. 592), but cheese topped frozen pizza does not sell well in St. Louis. (Patterson, Tr. 1782.) Kansas City is a "hamburger" market; General Mills was unsuccessful in entering the Kansas City market until it developed a hamburger pizza. (DeLapa, Tr. 1086–88.) Sausage pizza is the leading variety in St. Louis, even though it is close to the Kansas City "hamburger" market. (Smith, Tr. 1641.) [34]

121. Promotional allowances vary from market to market. (Carlson, Tr. 536–37; Francis, Tr. 669–70; Caron, Tr. 1018, 1034; DeLapa, Tr. 1218–20; Carpenter, Tr. 1336.) Different markets require different promotional and introductory programs because of the type of competitive activity in each market. (DeLapa, Tr. 1084–85; Barton, Tr. 1460–61.) Houston, Texas, is known as a free-goods market (*e.g.,*

one case free to a reseller with five purchased). (Carpenter, Tr. 1340–41; CCPF 142.)

122. Manufacturers concern themselves with and gather information regarding local and regional competitive conditions in the frozen prepared pizza business because of the distinct nature of competition and consumer preferences. (Nickel, Tr. 494.) Food brokers are relied upon to provide to frozen prepared pizza manufacturers regular, monthly, often weekly, information on competitors' prices, promotional activity, and new product introductions in each local market. (Carlson, Tr. 536–37, 548; Pizza, Tr. 703–04; Walling, Tr. 1277–80; Carpenter, Tr. 1334–36; Chamberlin, Tr. 1481–82; Patterson, Tr. 1746–48, 1753–54; Mosley, Tr. 1819–20.) Manufacturers also monitor local market activity by regular reviews of SAMI reports on each local market. (Pizza, Tr. 689; Malkowicz, Tr. 864–65; CCPF 144.)

123. Frozen prepared pizza manufacturers often tailor their promotional allowances and advertising efforts in a particular local market in response to promotions offered or advertisements run by one or more of their competitors in that local market. (As to promotions: Nickel, Tr. 440; Pizza, Tr. 709–10; Malkowicz, Tr. 861–62; Walling, Tr. 1298, 1300; Carpenter, Tr. 1337; Barton, Tr. 1445–46; As to Promotions and Advertising: DeLapa, Tr. 1084, 1112–13; CCPF 149.) [35]

Geographic Areas of Competition in the Frozen Prepared Pizza Industry

124. The parties agree that the United States as a whole is a relevant geographic market—the section of the country—within which Pillsbury's acquisition of Fox should be examined to determine the potential impact of the merger on competition (CCPF 120; RPF 79) but complaint counsel also contend that certain local metropolitan areas are relevant sections. (Complaint and Answer, ¶ 16; CCPF 121–23.)

125. Manufacturers of frozen prepared pizza in the United States have widely disparate distribution patterns. For example, one distributes coast to coast, but not border to border. (Pizza, Tr. 681.) Another distributes product in the States of Virginia, Colorado, Utah, Arizona, California and Hawaii. (Dursteen, Tr. 2337, 2338.) Yet another, having sales as far south as Miami, Florida, supplies product to that area from as far north as Duluth, Minnesota. (Malkowicz, Tr. 910; Carpenter, Tr. 1353.) Still another supplies pizza on a national basis, including Alaska, from a single plant in Salina, Kansas. (Miller, Tr. 977; Caron, Tr. 1023–24.) Even a small manufac-

turer like "Tree Tavern" can and does distribute product in three areas east of the Allegheny Mountains, Puerto Rico, and the U.S. Virgin Islands. (Francia, Tr. 1541-42; RPF 81.)

126. Many manufacturers are currently shipping product long distances and distribute product in a substantially nationwide pattern. Some manufacturers selling on a national basis ship frozen prepared pizza made at a single plant location. (Pizza, Tr. 679, 681, 731-34; Malkowicz, Tr. 898-901; Carpenter, Tr. 1353; Barton, Tr. 1434, 1440; Chamberlin, Tr. 1491-92; MacDonald, Tr. 2920, 2952-53; Cady, Tr. 3330; RX 1; RX 3; RPF 82.)

127. Transportation costs do not prevent frozen prepared pizza manufacturers who have only one or two manufacturing facilities from selling frozen prepared pizza anywhere in the United States. (Pizza, Tr. 734; Roxbury, Tr. 833; Barton, Tr. 1440; Cady, Tr. 3330-31; Malkowicz, Tr. 891-92; RX 7; RPF 89.) **[36]**

128. Buyers of pizza, located anywhere in the United States, can turn to manufacturers, located anywhere in the United States, for competitively priced products. (Cady, Tr. 3330, 3412-18, 3421-23, 3436-37; RPF 90.)

129. The manufacturers of Ellio's (Purex Corporation), Saluto (General Mills) and Stouffer's pizza not now in national distribution have present plans to achieve such distribution. (Malkowicz, Tr. 857, 891-92; DeLapa, Tr. 1072, 1134-35; Bard, Tr. 1704-05; MacDonald, Tr. 2921.) Ellio's (Purex) plans to expand its distribution to a nationwide level using two plants located 17 miles apart. (Malkowicz, Tr. 891-92; RPF 84.)

130. The only limitation on Pillsbury's geographical distribution of pizza has been its production capacity, which is insufficient to meet demand. (Francis, Tr. 612-20, 655; CX 27, p. 2; CX 7, p. 13; CX 6, p. 8.) This shortage in capacity is the reason that Pillsbury has not entered the trade areas of New England, New York and Los Angeles. (Nickel, Tr. 472; RPF 86.)

131. Since April 1976, utilizing one plant in Ohio, Ore-Ida, a subsidiary of H.J. Heinz Company (LaPizzeria brand), expanded its sales of frozen prepared pizza to the eleven cities or areas in the order listed: (1) Denver, (2) Chicago/Milwaukee, (3) Kansas City, (4) Des Moines, (5) Peoria, (6) Wichita, (7) Baltimore/Washington, (8) New Orleans, (9) Phoenix, (10) Tucson, (11) "the majority of the Northeast." (Rowlatt-Smith, Tr. 3767-68; RPF 87.)

132. Manufacturers of frozen prepared pizza recognize local grocery distribution areas as distinct and separate markets. (Boyce, Tr. 357-58, 362; Malkowicz, Tr. 873; Caron, Tr. 1002-03, 1043; DeLapa, Tr. 1099-1100; CCPF 135.)

133. Local marketing areas in which Fox and Totino's competed prior to the acquisition include: Houston, Dallas, and Lubbock, Texas; Tulsa, and Oklahoma City, Oklahoma; St. Louis, Kansas City, and Springfield, Missouri; Memphis, Tennessee; Little Rock, Arkansas; Atlanta, Georgia; North and South Carolina; Louisiana; Mississippi; Omaha, Nebraska; Montgomery and Birmingham, Alabama; and Denver, Colorado. (Boyce, Tr. 393; CCPF 122.) [37]

134. Localized geographic markets in which Pillsbury's Totino's and Fox competed prior to the acquisition and for which there are SAMI market share statistics available (CX 36 *in camera*) are:

1. Atlanta, Georgia
2. Charlotte, South Carolina
3. Dallas/Ft. Worth, Texas
4. Houston, Texas
5. Kansas City, Missouri
6. Memphis/Little Rock, Tenn., Ark.
7. Oklahoma City/ Tulsa, Oklahoma
8. Omaha, Des Moines, Neb. & Iowa
9. St. Louis, Missouri

(CCPF 123)

135. Forty-four percent of the total retail sales of Fox frozen prepared pizza sales, excluding private label sales, occurred in these nine market areas and 25% of the total retail sales of Totino's Frozen prepared pizza sales occurred in these markets in 1975 and 1976. (CX 36 *in camera;* CCPF 124.)

136. Industry recognized, local grocery distribution markets result from concentrations of food brokers, grocery buyers and warehouses. (DeLapa, Tr. 1218–20.) Local markets are "hubs of business"—population centers (Follansby, Tr. 1625), although they are not conducive to exact delineation by metes and bounds. (Caron, Tr. 1045.) They are, however, identifiable areas. (Nickel, Tr. 450–51.)

137. Usually, brokers acting as exclusive sales agents represent manufacturers within established territories. (Carlson, Tr. 586–87; Pizza, Tr. 702; Malkowicz, Tr. 884; DeLapa, Tr. 1096–97; Barton, Tr. 1391; Chamberlin, Tr. 1472–73.) Manufacturers of frozen prepared pizza often define local grocery distribution markets in terms of the boundaries of local food broker territories. (Pizza, Tr. 688; Carpenter, Tr. 1332, 1355, 1360; Barton, Tr. 1392; Chamberlin, Tr. 1473; CCPF 125.) [38]

138. The territory of food brokers is based, primarily on th location of retail food chain buying offices and wholesalers (DeLap

Tr. 1213-14; Barton, Tr. 1392; CCPF 127) and correspond to population centers, *e.g.,* St. Louis, Houston, or Kansas City, have been long-established, and are well-recognized in the grocery distribution trade. (Boyce, Tr. 353; Walling, Tr. 1328-29; Chamberlin, Tr. 1472-73; Patterson, Tr. 1738-39; CCPF 128.)

139. While the precise boundaries of various food broker territories in a given area may not coincide, they are generally similar (Carpenter, Tr. 1341; Mosley, Tr. 1824; Rosen, Tr. 885) and while differing slightly on the fringes, they share a core "city," *e.g.,* St. Louis, Houston, etc. (Follansby, Tr. 1625; CCPF 129.)

140. Food brokers "follow" retail grocery distribution patterns and service, *i.e.,* check displays, price markings, etc., even if a store of a chain is outside the broker's area of primary responsibility. (Pizza, Tr. 764, 777; Walling, Tr. 1291, 1315, 1328-29; Francia, Tr. 1544-45; RPF 94.)

141. Thus pizza sold by brokers within their areas of primary responsibility may be distributed by the purchasing reseller into the area of other brokers. The trade refers to this as competitive "spillover" or "overlap." (Nickel, Tr. 448; Pizza, Tr. 741, 764; Follansby, Tr. 1612; Walling, Tr. 1312-16, 1321, 1328-29; Barton, Tr. 1455; Francia, Tr. 1544-45; Coles, Tr. 1590; Patterson, Tr. 1758; Mosley, Tr. 1822; RX 10; RPF 95.)

142. Pizza distribution patterns and broker territories may or may not correspond to territories outlined by SAMI for its purposes. (Carlson, Tr. 571-72; Pizza, Tr. 742; Miller, Tr. 993; Caron, Tr. 1026; DeLapa, Tr. 1121-22; Patterson, Tr. 1742; Moore, Tr. 1806-07; Mosley, Tr. 1816-17; Barton, Tr. 1395-98; Rosen, Tr. 1883-84; Chamberlin, Tr. 1473-74; RPF 101.)

143. Some manufacturers have sales areas completely outside SAMI marketing areas. Others have sales areas which are partly within and partly outside such areas. SAMI determined that it would not be possible to encompass within the geographic boundaries of its areas all stores served by each reporting warehouse, because the listribution patterns of no two warehouses are precisely the same. CX 54, p. 8; Caron, Tr. 1027-28; DeLapa, Tr. 1182; Follansby, Tr. 624; RX 4; RPF 102.) [39]

The Plant Tour and Taste Test Conducted

144. As mentioned above (p. 9), a tour of the Fox Deluxe Pizza Co. ant in Joplin, Missouri, was taken. Frozen prepared pizza is anufactured there in the following manner which is typical: (1) ıgh is mixed, rolled out and cut into individual crusts; (2) the sts are then passed through an oven where they are partially

baked and cooled; (3) a tomato sauce and a meat or other topping is prepared separately and readied to be placed on the pizza; (4) the crusts are fed through a tomato sauce applicator; (5) cheese and some other toppings may also be applied either mechanically or by hand; (6) the fully garnished pizzas are then frozen in a blast (very quick-acting) freezer, packaged for sale, scanned electronically for foreign particles of metal and stored in a freezer until sold. (Balster and Spencer, Tr. 2150-2218; RPF 57.)

145. Also as a part of this proceeding, a taste test or competitive cutting, as is the custom in the trade, was held in an attempt to determine the similarities and differences in the various forms of pizza. (*See* RX 27 through RX 36, RX 27A through RX 36A, Tr. 2457-2538.) Pizza which came initially in a grocery shelf-stable, refrigerated, or frozen form, as well as pizzeria pizza was prepared according to package instructions or heated in the Pillsbury test kitchens. (*See* RX 24A - RX 36B.) The pizza samples served were not identifiable by type by the ALJ regardless of whether they initially were frozen, freshly baked or reheated, refrigerated, or grocery shelf-stable product. An exhibit (RX 24) shows the types tasted. It may be of interest that the ALJ only made one correct guess as to the type being tasted.

146. For a discussion as to the desirability and propriety of the trier of fact taking a tour of the Fox frozen prepared pizza manufacturing facility in Joplin, Missouri, and participating in the taste test in the Pillsbury kitchens in Minneapolis, Minnesota, *see* "Demonstrative Evidence," "McCormick on Evidence," "West Publishing Company, 2 ed., pp. 537-539." *Also see,* "Autoptic Proference," "Wigmore on Evidence," Chadbourn Revision, n.9, p. 388 and pp. 391-94. **[40]**

Barriers To Entering the Frozen Prepared Pizza Industry

147. A new plant designed to augment the production requirements of Pillsbury's Totino's brand pizza operation (which alread has a manufacturing facility at Fridley, Minnesota) would cost $1 million. (Levin, Tr. 239-40.) The cost of leasing a frozen prepar pizza production facility also is high: Purex paid $3 million to lea and improve its frozen prepared pizza facility which has a sin production line. (Malkowicz, Tr. 927; CCPF 164-165.)

148. In order to effectively compete in the frozen prepared p business, a company must advertise and promote extensi Economies of scale in advertising and production are necessa enter and become an effective competitor given the magnitude o other companies in the retail frozen prepared pizza business. (I

Tr. 248; DeLapa, Tr. 1084, 1103–04; Chamberlin, Tr. 1525–29; Horsch, Tr. 2710–11; CCPF 170.)

149. The expenditures for advertising and promotion are greater in gaining distribution of frozen prepared pizza than in any other frozen food category. (DeLapa, Tr. 1084.) Merely developing a good tasting product is not sufficient to enter the industry without extensive advertising and promotion. (Patterson, Tr. 1750–51.) Pillsbury recognized that expanding into new geographic areas, "dominated by well-established brands . . . will be extremely costly and represent[s] a drain on Divisional profit until the Totino's brand is well-established." (CX 2, p. 3, *in camera;* CCPF 172.)

150. The time period between entering the retail frozen pizza business and earning a normal return is long, and, therefore, a new entrant must be able to sustain losses over an extended interval. (Cady, Tr. 3379–81; CX 2, p. 96 *in camera;* CCPF 174.)

151. It is possible, though, to get into the business on a small scale with a total investment of about $50,000. (Stauffer, Tr. 2110; RPF 59.) [41]

Discussion

Elements of Section 7 of the Clayton Act

Section 7 (15 U.S.C. 18) provides that no corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital of another corporation engaged also in commerce, where in any line of commerce (the product market), in any section of the country (the geographic market), the ›ffect of the acquisition may be substantially to lessen competition, r to tend to create a monopoly.

Both Pillsbury and Fox were corporations engaged in commerce 'indings 1 and 2). That having been established, "determination of e relevant product and geographic market is 'a necessary predi- e' to deciding whether a merger contravenes the Clayton Act." *ited States* v. *Marine Bancorporation, Inc.*, 418 U.S. 602, 618 '4); *Brown Shoe Co.* v. *United States,* 370 U.S. 294, 324 (1962); *'ed States* v. *E.I. du Pont de Nemours & Co., et al.,* 353 U.S. 586, 1957).

The Product Market/The Line of Commerce

ıtification of the product market(s) affected by the acquisition first step to be taken in a Section 7 case in determining ·r a substantial lessening of competition has occurred or y will occur as a result of the acquisition. *Brown Shoe Co.,* *supra,* 370 U.S. at 324. In that leading case, the Supreme Court said that while there may be broad product markets whose outer boundaries "are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it . . .," there also may be "well defined submarkets" within the broader market which in themselves constitute product markets for antitrust purposes. Thus, men's, women's and children's shoes were held to be economically significant submarkets within the shoe industry — the broad product market. 370 U.S. at 325.

The court described seven factors which led it to distinguish the submarkets:

industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, [42] distinct customers, distinct prices, sensitivity to price changes, and specialized vendors . . . 370 U.S. at 325.

Thus, in cases decided subsequently such as *United States* v. *Aluminum Co. of America* (Alcoa-Rome), 377 U.S. 271 (1964), separate aluminum and copper submarkets were found to exist in the wire and cable industry and a separate paper insulated power cable submarket was found in *United States* v. *Kennecott Copper Corp.* (Kennecott), 231 F. Supp. 95, 98–100 (S.D.N.Y. 1964), *aff'd per curiam,* 381 U.S. 414 (1965). Even before *Brown Shoe,* it was held in *U.S.* v. *Bethlehem Steel Corp.,* 168 F. Supp. 576, 593–95 (S.D.N.Y. 1958), that while the iron and steel industry was the broad product market, ten specific items (*e.g.,* hot rolled sheets, track spikes, electricweld pipe, oil field equipment and supplies) comprised identifiable product submarkets as well.

Decisions such as *Alcoa-Rome, Kennecott,* and many others which came after *Brown Shoe* have made it clear that not all or even most of the seven factors need to be present before a valid submarket for Section 7 purposes may be found to exist. *Liggett & Myers, Incorporated* v. *FTC,* 567 F.2d 1273, 1274–5, (4th Cir. 1977); *United States* v. *Phillipsburg National Bank & Trust Co.,* 399 U.S. 350, 359–60 (1970); *United States* v. *Continental Can Co.* (Continental Can), 378 U.S. 441, 456–57 (1964); *Columbia Broadcasting System, Inc.* v. *FTC,* 414 F.2d 974, 979 (7th Cir. 1969), *cert. denied,* 397 U.S. 907 (1970); *General Foods Corp.* v. *FTC,* 386 F.2d 936, 941 (3rd Cir. 1967); *Reichold Chemicals, Inc.,* Dkt. 9076, p. 63, Initial Decision, Commission Opinion, slip copy, dated February 22, 1978 [91 F.T.C. 246]; *U.S.* v. *Mrs. Smith's Pie Co.,* 1977-1 CCH, Trade Cas. ¶61,518 (E.D. Pa. Nov. 19, 1976) at 72,021-3.

Counsel for Pillsbury contends that only the broad market, pizza

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be it prepared frozen (*e.g.*, completely prepared except for heating), refrigerated (*i.e.*, requiring a combination of various components plus heating), shelf-stable (*i.e.*, dry and requiring mixing of ingredients and the combination of components plus cooking) or carry-out from a pizzeria restaurant (*i.e.*, ready-to-eat), is the relevant line of commerce. He also suggests that the market includes such products as frozen TV dinners and other frozen entrees, other carry-out foods, etc. (Respondents' Brief, pp. 8-13.) [43]

I do not agree, even though in an appropriate case the broad market — pizza in its various forms — might be examined as the relevant line of commerce. *See Continental Can, supra,* 378 U.S. at 456-58. There is ample, convincing evidence to establish that frozen prepared pizza is the relevant product market and that this case is not appropriate for an examination of the additional products counsel for Pillsbury proposes.

The evidence here shows that frozen prepared pizza is recognized by the food industry as being separate and distinct. The manufacturers, as do the brokers normally employed for distribution of frozen prepared pizza to resellers, so consider it. (Findings 66, 67, 70-73.) In addition, producers/manufacturers of frozen prepared pizza look at the activity/business operations of other such producers in deciding their competitive actions. (Findings 58-62.) There is an association of frozen prepared pizza manufacturers. (Finding 54.) Further, frozen prepared pizza has peculiar characteristics due to its manner of preparation, state of completion and manner of preservation. Also frozen prepared pizza is sensitive primarily to changes in the price of other frozen prepared pizza. (Findings 38-41, 50, 57, 68, 117.) Lastly, frozen prepared pizza is made on machinery, sometimes custom-designed, which is different from that used to make other types of pizza by producers who concentrate on the manufacture of frozen prepared pizza as distinguished from pizzeria, shelf-stable and refrigerated pizza. (Findings 44, 51, 55.) It also is appropriate to mention that simply because the administrative law judge only ;uessed right once in the taste test (Finding 145) the fact is of no :onsequence in determining the relevant product market in this ase.

The frozen prepared pizza market is "sufficiently inclusive to be ıeaningful in terms of trade realities." *Crown Zellerbach Corporaon* v. *FTC,* 296, F.2d 800, 811 (9th Cir. 1961) and it is proper to ınsider frozen prepared pizza as the relevant line of commerce in nnection with determining whether the acquisition of Fox by llsbury violated Section 7. [44]

2. The Geographic Market/The Section of the Country

The section(s) of the country or geographic market(s) one must examine in order to determine whether an acquisition has or probably will substantially lessen competition is(are) identified in much the same way as the product market. Thus, in *Brown Shoe, supra,* 370 U.S. at 336–37, the Supreme Court said that the "criteria to be used in determining the appropriate geographic market are essentially similar to those used to determine the relevant product market. . . . The geographic market selected must . . . both correspond to the commercial realities of the industry and be economically significant. . . . [A]lthough the geographic market in some instances may encompass the entire Nation, in some other circumstances, it may be as small as a single metropolitan area."

Particularly clear from *Brown Shoe* and other precedents is that in a case such as this the section of the country to be examined need not be marked off in metes and bounds. *United States* v. *Pabst Brewing Co.,* 384 U.S. 546, 549 (1966); *E.I. du Pont & Co., supra,* 351 U.S. at 395. In connection with identification of regional markets, in *Philadelphia National Bank,* 374 U.S. at 360 n.37 (1963), the Supreme Court said:

> . . . there is still some artificiality in deeming the four county area the relevant 'section of the country' so far as businessmen located near the perimeter are concerned. But such fuzziness would seem inherent in any attempt to delineate the relevant geographical market.

Also see United States v. *Connecticut National Bank,* 418 U.S. 656, 669–70 (1974), where the Court said that it is the Government's role to come forward with evidence "delineating the rough approximation of localized banking markets mandated by *Phildelphia Bank, supra,* and *Phillipsburg National Bank, supra.*"

The effects of an acquisition have been considered by the Supreme and lower Courts with reference to both broad geographic markets and submarkets within the broad area, in basically the same manner as in the case of product markets. *United States* v. *Kimberly-Clark Corp.,* 264 F. Supp. 439, 455–56 (N.D. Cal. 1967); *United States* v. *Bethelehem Steel Corp., supra,* 168 F. Supp. at 601–02. [45]

In *Marine Bancorporation, supra,* 418 U.S. at 620–21, where potential rather than, as here, horizontal competition was involved, the Supreme Court held that "without exception the Court has treated 'section of the country' and 'relevant geographic market' as identical, and it has defined the latter concept as the area in which the goods or services at issue are marketed to a significant degree by the acquired firm." In commenting on the "section of the country" holding of the Court in *Pabst Brewing, supra,* 384 U.S. at 550–51, the Court said in *Marine Bancorporation* in footnote 20:

> Some of the Court's language in *Pabst* suggests that the Government may challenge a merger under § 7 without establishing any relevant geographic market. . . . But Pabst in reality held that the Government had established three relevant markets in which the acquired firm actually marketed its products—a single State, a multistate area, and the Nation as a whole. . . . And in that case the acquiring firm was an actual competitor of the acquired firm in all three relevant geographic markets. . . . Thus while *Pabst* stands for the proposition that there may be more than one relevant geographic market, it did not abandon the traditional view that for purposes of § 7 "section of the country" means "relevant geographic market" and the latter concept means the area in which the relevant product is in fact marketed by the acquired firm.

Under these criteria, in this case both the United States as a whole and those regional areas of the United States in which Pillsbury and Fox competed could be examined as the relevant sections of the country. As noted, counsel agree on the national geographic market but disagree as to whether local geographic markets also should be considered.

Complaint counsel contend that several regional areas comprised of metropolitan centers of the United States are also relevant sections of the country. (Complaint ¶ 19.) They may be but the evidence does not establish the fact sufficiently. For example, there is no evidence that customers are limited by circumstances or limit themselves to sellers located in any meaningful geographic area other than the United States as a whole. Even if the proposed/alleged regions were accepted as relevant geographic markets, the evidence does not establish that any of them is effectively insulated from outside competitive forces which the Commission has said is an important distinguishing characteristic. *Jim Walter Corp.,* Dkt. 8986, 3 CCH TRR ¶ 21,379 at 21,316, December 20, 1977 [90 F.T.C. 671].

It is well established that Section 7 of the Clayton Act does not require precise mathematical certainty in the ascertainment of market size and market share, *Brown Shoe, supra,* 370 U.S. at 341–42, n.69, but more is needed than we have here to support a conclusion as to regional markets. [46]

The U.S. District Court, in *U.S.* v. *Mrs. Smith's Pie Co., supra,* 1977-1 CCH Trade Cas. relied on SAMI statistics to make a determination as to the national market shares concluding, and I agree, that SAMI data/evidence is reasonable, credible and reliable for such use at ¶61,518 p. 72,017.

In 1976, Pillsbury and Fox competed in selling frozen prepared pizza in thirteen, widespread states, from Alabama to Colorado

(Finding 133). Frozen prepared pizza is distributed nationally. The major firms compete with others throughout the United States (Findings 126-131). These facts warrant considering the nation as a whole as a relevant geographic market. *See* Commission Opinion in *Jim Walter Corporation, supra,* Dkt. 8986, 3 CCH TRR at 21,313-16. This conclusion is reinforced by the fact that the parties agree on the Nation as the relevant geographic market. (Finding 124).

Even though Pillsbury and Fox did not actually sell their frozen prepared pizza in every state, there are numerous precedents to the effect that a national market may be considered in the circumstances obtaining here. *See FTC* v. *Procter and Gamble Co.,* 386 U.S. 568, 571-72 (1967); *Pabst, supra,* 384 U.S. at 549-51; *A.G. Spalding & Bros., Inc.* v. *FTC,* 301 F.2d 585, 607 (3d Cir. 1962); *Kimberly-Clark, supra,* 264 F. Supp. at 454-58.

In *Kennecott Copper Corp.,* Dkt. 8765, 78 F.T.C. 744 at 917-18 (May 5, 1971), the Commission said that a national market existed for coal even though the acquired firm (Peabody Coal Company) sold principally in the North and South Central States and there was no evidence of sales in the Northeast, Mid-Atlantic or Northwestern States, *aff'd,* 467 F.2d 67 (10th Cir. 1972), *cert. denied,* 416 U.S. 909 (1974), *rehearing denied,* 416 U.S. 963 (1974). *Also see United States* v. *Jos. Schlitz Brewing Company,* 253 F. Supp. 129 at 134-35 (N.D. Cal. 1966).

Consequently, and as is alleged in the complaint (¶ 16), the United States as a whole is the relevant section of the country for consideration in this case. [47]

3. Market Concentration

The Congress made it clear that its primary concern when the Clayton Act was amended was to forestall, insofar as possible, reductions in competition in all lines of commerce by keeping a large number of small competitors in business. *United States* v. *Von's Grocery Co.,* 384 U.S. 270, 275 (1966). More recently, the Supreme Court in *Phildelphia National Bank, supra,* 374 U.S. at 363, as quoted in *United States* v. *General Dynamics Corp.,* 415 U.S. 486 at 497 (1973), said:

> This intense congressional concern with the trend toward concentration warrants dispensing, in certain cases, with elaborate proof of market structure, market behavior, or probable anticompetitive effects. Specifically, we think that a merger which produces a firm controlling an *undue* percentage share of the relevant market, and results in a *significant* increase in the concentration of firms in that market, is so inherently likely to lessen competition substantially that it must be enjoined *in the*

absence of evidence clearly showing that the merger is not likely to have such anticompetitive effects. [Emphasis added]

In Section 7 cases market shares are the primary indicia of market power, but it is also necessary to examine the structure, history, and probable future of the particular market. *U.S.* v. *Continental Can Co.*, 378 U.S. at 458 (1964). (RPF p. 124.)

Competition in the manufacture of frozen prepared pizza is intense and probably will continue to be so. (Findings 107, 110–13, 115.)

In *Stanley Works* v. *FTC*, 469 F.2d 498, 504 (2nd Cir. 1972), *cert. denied*, 412 U.S. 928 (1973), the court said that the cabinet hardware industry was concentrated because the 4-firm percentage of market was 49 percent to 51 per cent. To the same effect, in *Industrial Organization*, Professor Joe Bain says that a market in which the 4-firm percentage is 50 percent reflects high-moderate concentration (p. 31, 2d ed. 1968). After Pillsbury acquired Fox 4-firm concentration was 63.23% in 1975 and 62.53% in 1976. (Finding 105.) However, the merger in this proceeding does [48] not fall within the class of horizontal mergers, ordinarily subject to challenge under the Department of Justice Merger Guidelines. (1 Trade Reg. Rep., ¶4510 at 6884.) Neither in 1976 nor in 1975 did Fox, with its 1.7% and 2.4% market share (see next paragraph) come up to the Department's criteria of the acquired firm having 2% or more if the acquirer had at least 20% (1976) or less than 2% if the acquirer had 25% (1975). (Findings 103, 104.)

The evidence here shows that based on SAMI data national 4-firm and 8-firm concentration was about 62% and 84% respectively in 1976 (Finding 105) and that nationally Fox and Pillsbury had market shares of: Fox 1.7% in 1976 and 2.4% in 1975; Pillsbury 17.1% in 1976 and 16.1% in 1975. (Findings 103, 104.)

Counsel for Pillsbury questions the use of the SAMI data offered by complaint counsel to show these market shares (RB, pp. 24–35) but I am convinced that it is probative evidence in this case. Even though SAMI data is not as precise as some other sources of such information might be (*e.g.*, a Commission Section 6(b) survey) industry member reliance on it persuades me that it is more than adequate for our purposes. This is because the data provides a sufficiently reliable indication of the market shares of various brands of frozen prepared pizza due to SAMI's extensive coverage of the warehouses through which frozen prepared pizza travels in reaching the retailer. Even if it is possible to point to technical flaws in the compilation of industry statistics, the Supreme Court has held that "precision in detail is less important than the accuracy of the broad picture presented." *Brown Shoe, supra*, 370 U.S. at 342 n.69.

Although the SAMI data lack precision in detail when compared with what other techniques for measuring market shares might provide, the SAMI data is probative evidence. Certainly those most qualified, the businessmen concerned with sales of frozen prepared pizza — including Pillsbury — say so by subscribing to the service and relying on it. (Findings 79–83, 85, 95–97.)

The Commission also has said there is no requirement that the exact size of a product market need be shown in a Section 7 case. *Papercraft Corp.*, Dkt. 8779, 78 F.T.C. 1352, 1405–06 (1971), *modified and aff'd*, 472 F.2d 927 (7th Cir. 1973). The SAMI data amply present the "picture" of the sales of frozen prepared pizza in the Nation — the relevant section of the country which has been shown to exist. [49]

As a matter of first impression, this case does appear to be governed by the principles that (1) where there has been a "history of tendency toward concentration in the industry," tendencies toward further concentration "are to be curbed in their incipiency." *Continental Can, supra*, 378 U.S. at 461, citing *Brown Shoe, supra*, 370 U.S. at 345–46, and (2) where "concentration is already great the importance of preventing even slight increases in concentration and so preserving the possibility of eventual deconcentration is correspondingly great." *Philadelphia National Bank, supra*, 374 U.S. at 365 n.42. As a predicate, however, each of these cases had the fact that a *substantial* actual or probable lessening of competition had or would occur. That predicate is missing here. Here, there is convincing evidence that the acquisition did not, and probably will not, result in a substantial lessening of competition. This evidence is discussed under the caption "Competitive Effects." As to the importance of considering such evidence, *see* the Commission's Opinion in *Coca-Cola*, Dkt. 8855, p. 87, April 7, 1978 and reference there to the *Jim Walter* opinion, *supra*.

4. Ease of Entry

Counsel for Pillsbury presented evidence to show that there are no significant barriers to entry into the frozen prepared pizza industry because (1) a plant making frozen prepared pizza can be constructed for very little money or even started in a garage, (2) technological requirements are minimal, (3) the machinery needed is available at reasonable prices, (4) start-up advertising by a small entrant is not important in the industry, (5) small firms do well, and (6) there are ready means of distribution open to new entrants. The evidence as to difficulty of entry, however, (Findings 147–151) outweighs that presented by counsel for Pillsbury. Although I agree with the position of counsel for Pillsbury to the effect that the evidence he presented is germane to questions as to the various aspects of an acquisition, including the probability of adverse competitive effects, that does not negate the fact that in this acquisition, competition between Pillsbury and Fox in a number of sections of the country was eliminated.

Most persuasive however is the fact that ease of entry in and of itself is not an effective defense to a charge that competition has been eliminated. In *Ekco Products Co.,* Dkt. 8122, 65 F.T.C. 1163, at 1208 (1964), *aff'd,* 347 F.2d [50] 745 (7th Cir. 1965), the Commission said:

> . . . where the merger's effects on competition are those prescribed by Section 7, its illegality cannot be overcome by a showing of ease of entry. . . . Ease of entry may, to be sure, cause the market power of established firms to be eroded by the advent of significant new competitors; but that is likely to be at best a long-term affair. . . . In short, the absence of high entry barriers cannot be depended upon to ensure effectively competitive conditions. . . . [and] a merger that has been proved to be so anticompetitive as to violate Section 7, even apart from difficulty of entry into the market, cannot be defended on a mere showing of absence of high entry barriers.

See Bok, *Section 7 of the Clayton Act and the Merging of Law and Economics,* 74 Harvard L. Rev. 226–260 (1960). . . . *Cf.* Bain, Barriers to New Competition 189 (1956); Bain, Industrial Organization 425 (1959).

Also see American Brake Shoe Co., Dkt. 8622, 73 F.T.C. 610, 684 (1968).

In a "horizontal" Section 7 case, the focus is on the existing and future *competition* affected by the firms involved in the merger rather than on the potential for additional competition provided by new entrants into the industry. Thus, the contentions of counsel for Pillsbury regarding ease of entry have not been persuasive in deciding this case but his arguments as to the probable competitive effects have been convincing.

5. Competitive Effects

A basic premise of Section 7 is that competition will be most vital when there are many sellers, none of which has any significant market share. *Philadelphia National Bank, supra,* 374 U.S. at 363; *Alcoa-Rome, supra,* 377 U.S. at 289. The *ultimate* question to be addressed is [51] whether the acquisition/merger has or probably will *substantially* lessen competition in the relevant product and geographic markets. Section 7 was particularly directed against elimination of horizontal competition which was significant and would probably continue to be so in the future. And it has been recognized for a long time that the policy underlying the Section "is that corporate growth by internal expansion is socially preferable to growth by acquisition." *Philadelphia National Bank, supra,* 374 U.S. at 370; *accord, Ekco Products, supra,* 347 F.2d 745, at 752.

Pillsbury and Fox were competitors in the frozen prepared pizza industry and Pillsbury clearly had an appreciable market share nationally. Fox did not. (Pillsbury *13.7%;* Fox *2.4%* in 1975.) (Finding 104.) The acquisition of Fox by Pillsbury did eliminate an independent competitor with the result that the buying options available to reselling and other purchasers of frozen prepared pizza were reduced by one due to Fox having been eliminated as an independent source of supply. (Findings 34, 102.) Even so, the acquisition did not *substantially* lessen competition and probably will not do so in the future.

The Supreme Court has ruled that acquisitions of competitors with even lower industry rankings than those of Pillsbury and Fox are illegal. One example, is *Brown Shoe, supra,* where the combined market share was over 5 percent, 370 U.S. 341–43. In *Alcoa-Rome, supra,* 377 U.S. at 271, acquisition of the ninth ranked firm, with 1.3 percent of the aluminum conductor market, *by the market leader* with a 27.8 percent market share was found to be unlawful. Similarly, a merger between the *sixth and seventh* ranked firms, Blatz with 5.84 percent and Pabst with 5.48 percent, respectively, of the three-state beer market in *Pabst, supra,* 384 U.S. at 551–52, violated Section 7. Also, with a combined market share of 8.9 percent, a merger between the *third-ranking firm* with 4.7 percent and the *sixth-ranking firm* with 4.2 percent of the retail grocery market in the Los Angeles area was held in *Von's Grocery, supra,* 384 U.S. at 281, to violate Section 7. [52]

Instead of growing by expanding internally with the possibility of market deconcentration, Pillsbury combined with Fox and if the competition involved were different a violation of Section 7 would have resulted. The merger of Pillsbury and Fox was decided upon to solve the pressing production problem which Pillsbury had and enabled Pillsbury to more nearly meet its production needs and most important from the standpoint of Section 7 to enter into competition in an already concentrated industry in new geographic areas which Fox had been unable to enter. (Findings 35, 130, 149.) The acquisition created more jobs in the Fox production plant (Finding 14), upgraded the physical condition of those facilities through substantial investment of capital (Finding 15), and made for a more viable, intensive, competitive situation in the frozen prepared pizza industry than would have been the case if Fox had continued as a separate entity. (Findings 111, 112.) Consequently, the acquisition did not and probably will not have the substantial adverse effects on competition which the Congress was addressing when Section 7 was enacted in 1914 and amended in 1950.

Complaint counsel met prima facially, the burden of proving that the effect of the acquisition would be substantially to lessen competition. He showed this by establishing that the Nation and that frozen prepared pizza are the relevant markets and then introducing statistical evidence to show the market shares held by the parties and other industry leaders. *But* such statistical evidence has never constituted more than "*prima facie*"proof of a violation of Section 7. *Jim Walter Corp.,* Commission Opinion in Dkt. 8986, 3 CCH TRR ¶ 21,379, p. 21,320, Dec. 20, 1977. Market shares are the primary indicia of market power, *United States* v. *Continental Can Co., supra,* 378 U.S. at 458. However, a further examination of the structure, history and probable future of the applicable market is necessary. *Jim Walter Corp., supra,* 3 CCH TRR at p. 21,316. (RPF 132.)

In *General Dynamics* as the Commission noted in *Jim Walter Corp., supra,* 3 CCH TRR at 21,317, "after a further examination of the 'structure, history and probable future' of the coal industry the Court concluded that [53] despite high levels of concentration in the industry other factors justified the conclusion that the acquisition would not have the requisite anticompetitive effect." (RPF p. 132.)

In *U.S.* v. *General Dynamics,* 415 U.S. 486 at 498 (1974), the Supreme Court upheld a district court's finding that, despite statistical market shares which appeared to show a concentrated market and an increased market share resulting from the acquisition, "other pertinent factors" affecting the industry and the business of the parties led to the conclusion that no substantial lessening of competition had occurred or was threatened by the acquisition.

There the evidence showed that: (a) coal was sold principally pursuant to long-term contract; (b) a producer's ability to compete in the future turned on whether or not it had the necessary reserves to negotiate new contracts; (c) although the acquired firm was financially healthy, by the time of suit its uncommitted reserves of recoverable coal were very low, and it was not in a position to increase them; and (d) as a result, the acquired firm could not compete effectively for long-term contracts and, accordingly, was "a far less significant factor in the coal market than the Government contended or the production statistics seemed to indicate." 415 U.S., at 499-504. "Irrespective of the company's size when viewed as a producer, its weakness as a competitor was properly analyzed by the District Court and fully substantiated that court's conclusion that its acquisition by Material Service would not 'substantially . . . lessen competition.' " 415 U.S., at 503-04.

The Court accepted the lower court's holding that there is a defense other than that the acquiree was failing to a charge that Clayton Section 7 has been violated.

Pillsbury's Failing Company Defense

One defense to a charge that Section 7 has been violated stems from language in *International Shoe Co.* v. *FTC*, 280 U.S. 291, 301-303 (1930). There the Supreme Court said:

> It is perfectly plain from all the evidence that the controlling purpose of the International in making the purchase in question was to secure additional factories, which it could not itself build with sufficient speed to meet the pressing requirements of its business.
>
> * * * * * * *
>
> [54] Shortly stated, the evidence establishes the case of a corporation in failing circumstances, the recovery of which to a normal condition was to say the least, in gravest doubt, selling its capital to the only available purchaser in order to avoid what its officers fairly concluded was a more disastrous fate. It was suggested by the court below, and also here in argument, that instead of an outright sale, any one of several alternatives might have been adopted which would have saved the property and preserved competition; but, as it seems to us, all of these may be dismissed as lying wholly, within the realm of speculation.
>
> * * * * * * *
>
> In the light of the case thus disclosed of a corporation with resources so depleted and the prospect of rehabilitation so remote that it faced the grave probability of a business failure with resulting loss to its stockholders and injury to the communities where its plants were operated, we hold that the purchase of its capital stock by a competitor (there being no other prospective purchaser), not with a purpose to lessen competition, but to facilitate the accumulated business of the purchaser and with the effect of mitigating seriously injurious consequences otherwise probable, is not in contemplation of law prejudicial to the public and does not substantially lessen competition or restrain commerce within the intent of the Clayton Act. To regard such a transaction as a violation of law as this Court suggested in *United States* v. *U.S. Steel Corp.*, 251 U.S. 417, 446-447, would "seem a distempered view of purchase and result." See also *American Press Ass'n* v. *United States*, 245 Fed. 91, 93-94.

[55] At that time Section 7 applied to lessenings of competition between the acquiring and acquired corporations. The Section was amended in 1950 to apply to lessenings of *competition* in any line of commerce.

Both houses of the Congress sanctioned the defense when Section 7 was amended in 1950 (H. Rep. No. 1191, 81st Cong., 1st Sess., 6 (1949): S. Rep. No. 1775, 81st Cong. 2d Sess., 7 (1950) as follows:

Companies in a failing or bankrupt condition

* * * * * * *

[T]he [Supreme] Court has held . . . that a company does not have to be actually in a state of bankruptcy to be exempt from its [Section 7's] provisions; it is sufficient that it is heading in that direction with the probability that bankruptcy will ensue.

* * * * * * *

It is expected that, in the administration of the act, full consideration will be given to all matters bearing upon the maintenance of competition, including the circumstances giving rise to the acquisition.

The "Report of the Attorney General's National Committee to Study the Antitrust Laws" (1955) also notes the existence of the failing company defense by reference to both *International Shoe* and the Congressional reports cited above (p. 123).

The requirements for establishing the defense were refined in *Citizen Publishing Co.* v. *United States,* 394 U.S. 131 (1969). There in holding that the defense had not been established the Court said that it had no occasion to determine what changes, if any, the 1950 amendment had on the failing company doctrine (n.3 at 137). The facts were that two newspapers — the Tucson Arizona Citizen and the Star — combined their business operations while maintaining separate news and editorial departments. The Court said that the ostensibly failing, merged corporation was not on the [56] verge of going out of business, that there was no serious probability that it would terminate its business and liquidate its assets unless the merger ("the last straw") was effected, that attempts to sell the firm never had been made and that the "failing" newspaper continued to be a significant threat "to the Star" (394 U.S. at 137). The Court added that the prospect of reorganization under Chapter XI of the bankruptcy Act ". . . would have had to be dim or nonexistent to make the failing company defense applicable. . ." (at 138) and that "We confine the failing company doctrine to its present narrow scope" (at 139).

Most recently — in an opinion dated February 22, 1978 — the Commission commented on the "failing company" defense when it adopted the initial decision of Administrative Law Judge (ALJ) Morton Needelman in *Reichhold Chemicals, Inc.*, Dkt. 9076 (July 19, 1977) [*supra*]. There the ALJ found that the "failing company" criteria had not been shown because Reichhold *met none of the* *requirements.* (n.92, p. 72, Initial Decision, slip copy). The defense was based on the fact that the acquired firm was weak and that *Reichhold discarded the acquired company* because it failed" . . . to come up to *Reichhold's* intra-corporate standards for profitability and efficiency" (p. 72, Initial Decision, slip copy). There is much evidence in this case as to Fox's poor financial condition and there is no evidence that Pillsbury intends to discard Fox. If there was, my attitude toward the acquisition would be much different.

The Reichhold decision continued:

> There is no such quasi-failing company defense available under Section 7 of the Clayton Act. The market is supposed to determine whether firms fail or not, and the very purpose of the "failing company" doctrine is to preserve (and not discard as Reichhold did) an entity which would have collapsed but for the acquisition. *International Shoe Co.* v. *FTC,* 280 U.S. 291 (1930). As for the use by a large firm of *its* internal standards to determine whether a [57] small competitor fails or not, the legislative history of Section 7 indicates that the Congressional intent was just the opposite — Congress wanted to stop acquisitions which give large firms discretionary power over the continued development or, for that matter, the existence of their smaller competitors. *Crown Zellerbach Corp.* v. *FTC,* 296 F.2d 800 (9th Cir. 1961), *cert. denied,* 370 U.S. 937; see also concurring opinion of Mr. Justice Douglas in *United States* v. *Falstaff Brewing Corp.,* 410 U.S. 526, 538 (1973). At 72.

Counsel for Pillsbury then has not made out the failing company defense. Fox had not yet reached the extreme financial distress situation which these decisions suggest must be present for the defense, in and of itself, to insulate the acquisition from being found to be a violation of Section 7. But its precarious position when considered in the light of other factors convinces me that the acquisition did not violate Clayton Section 7, or consequentially FTCA Section 5.

Pillsbury's No-Public-Interest Defense

Counsel for Pillsbury contends that this proceeding is not in the public interest (RB, pp. 46–50). This is because, in summary, Fox's plant was not operated in accord with U.S.D.A. and other federal regulations affecting health and safety and Pillsbury was able to and did correct the deficiencies.

These points raised by counsel for Pillsbury do have a bearing on the "General Dynamics" defense discussed below because they address the question of whether Fox indeed was or probably would be able to have an impact on competition in the frozen prepared pizza industry.

Insofar as the points are intended to address a no-public-interest defense, however, the Commission has said that question is reserved to itself and that it is not to be ruled upon by the administrative law judge. In [58] deciding to issue a complaint, the Commission proper, in accord with Section 5(b) of the FTC Act, determines that it has "reason to believe" that the proceeding is "to the interest of the public." Two holdings by the Commission to this effect are *Exxon Corp.*, 83 F.T.C. 1759 (1974) and *Herbert R. Gibson, Sr., et al.*, Dkt. 9016, October 12, 1977.

Lastly, respondents conceded that entry of the court's order was in the public interest when it entered into a stipulation with Commission attorneys in connection with settlement of the Commission's suit for a preliminary injunction. (See p. 3 above.) If entry of the order after the preliminary injunction to stop the acquisition of Fox by Pillsbury and agreeing to the terms of the preliminary injunction issued are in the public interest, it follows that these administrative proceedings are "to the interest of the public"—the language of FTCA Section 5. [59]

The General Dynamics Defense

An appellate court decision on November 4, 1977, in *United States* v. *International Harvester Company,* 564 F.2d 769 (7th Cir. 1977) upheld a district court opinion (U.S.D.C., No. Dist. of Illinois, Eastern Division — the same court which issued the preliminary injunction in this case — see p. 2, above) in which the "General Dynamics" defense 415 U.S. 486 (1974) was established. The circuit court said (564 F.2d at 773) that evidence of the acquired firm's "weakness as a competitor" properly was considered by the district court as rebuttal to the government's statistical evidence which had established that the acquisition was presumptively illegal. See *Marine Bancorporation, supra,* 418 U.S. at 631.

Even accepting the statistics as the primary index of market power "only a further examination of the particular market — its structure, history and probable future — can provide the appropriate setting for judging the probable anticompetitive effect of the merger." *Brown Shoe,* 370 U.S. at 322, n.38, quoted in *General Dynamics,* 415 U.S. at 498.

The evidence in *International Harvester* showed that even if the acquired firm had remained in the market ". . .it did not have sufficient resources to compete effectively, and this supports the district court's conclusion that the acquisition of 39 percent of Steiger's stock by Harvester would not substantially lessen competition. See [*General Dynamics*] 415 U.S. at 508, 509-510, 94 S. Ct. 1186." 564 F.2d at 774.

The evidence here shows that Fox in an intensely competitive industry dominated by large firms, was financially weak, had production problems requiring capital for investment Fox did not have, could not offer advertising assistance or other promotions which successful competition in the frozen prepared pizza industry demands and had a division which even complaint counsel's witness said was debilitating Fox and on the sale of which the witness' testimony as to Fox's viability hinged. (Findings 110-113; 15-17, 19-27, 30-32.)

Footnote 7 (564 F.2d 773) of the *International Harvester* opinion elaborates on the thinking of the circuit court:

Although the Government asserts that *General Dynamics* is distinguishable on the facts (Br. 22 n.20, Reply Br. 11 n.9), the rationale of that [60] case was not limited to situations involving limited amounts of a natural resource, such as the coal reserves at issue there. On the contrary, in a rapidly expanding industry in which plant expansion and an ability to keep pace with demand are as Judge Leighton concluded, "needed * * * to take advantage of the growing * * * market" (finding 33), current sales and production, taken apart from the availability of capital, are no less "unreliable indicators of actual market behavior," *United States* v. *Marine Bancorporation, supra,* at 631, 94 S. Ct. at 2875, than production was in *General Dynamics* when taken apart from coal reserves. Moreover, the type of evidence that the Supreme Court itself has considered after *General Dynamics* (see *United States* v. *Citizens & Southern National Bank, supra,* at 121, 95 S. Ct. 2099; *United States* v. *Marine Bancorporation, supra,* at 631-632, 94 S. Ct. at 2874-2875) indicates that the "*General Dynamics* defense" is not to be limited to the absence of resources, either natural or monetary, but rather should include, at least as the Government admits elsewhere in its brief, those "special circumstances" in the case that indicate that the "statistical data did not provide a reliable indication of the future effect of the acquisition" (Br. 19 n.18), or perhaps even more broadly, any evidence indicating that statistical projections may be unreliable, *cf. United States* v. *Amax, supra,* 402 F. Supp. at 970.

As indicated above (Findings 14-17, 19-32; 35), the Pillsbury-Fox situation is analogous in a sufficient number of ways to convince me that the *International Harvester* decision is precedential to this case. [61]

To the same result are a number of Commission decisions in response to requests for advisory opinions. These indicate that an acquisition was approved when it apparently was improbable that substantial, adverse effects on competition would ensue:

(1) A large diversified manufacturer was granted clearance to acquire the second largest integrated manufacturer of a specialty closure product. The top four firms accounted for 55% of the market and the acquiree was in poor financial condition. Advisory Opinion Digest 169; 1 CCH TRR ¶ 4295.98.

(2) Clearance was granted to acquire a deteriorating competitor doing business in a limited geographical area by a firm

operating nationally after reasonable but unsuccessful efforts had been made to find another buyer. Advisory Opinion Digest 165; 1 CCH TRR ¶ 4295.07.

(3) Two large food processors subject to an order requiring prior approval were permitted to acquire a small food processor which had declining profits, too small a plant and the owner was determined to sell. Advisory Opinion Digest 185; 1 CCH TRR ¶ 4295.17.

Also see Advisory Opinion Digests 177 and 179; 1 CCH TRR ¶ 4295.35, "Equities." **[62]**

The Section 5(a)(1) Charges in the Complaint

As noted in the beginning of this initial decision (p. 1) the complaint alleged that both Clayton Section 7 and FTCA Section 5 were violated by Pillsbury and Fox by (1) consummation of the acquisition and (2) by having contracted to make the acquisition. Since these allegations hinge on the Section 7 aspects and have not been separately addressed by argument or evidence offered there is no basis for finding that FTCA Section 5 was violated as alleged.

Respondents Request for Attorneys Fees and Costs

With regard to respondent Pillsbury's request for attorneys fees and costs (p. 4) above; Answer, last par., p. 5) there is no provision in the Commission's adjudicative (Part 3) rules for such payments. There is a provision in Part 1, Section 1.17 "Compensation for representation in rulemaking proceedings," that is grounded on inability of a person having a legitimate interest in the trade regulation rule proceedings to participate ". . .because such person cannot afford to pay costs. . ." (subparagraph (a) of Section 1.17). Clearly, the provision does not apply to adjudicative proceedings or to a respondent such as Pillsbury. *See also,* "Magnuson-Moss Warranty—Federal Trade Commission Improvement Act," 15 U.S.C. 2310(a)(5)(d)(2).

Conclusions

1. The Commission has jurisdiction of and over the respondents, the subject of this proceeding and the proceedings were and are to the interest of the public.
2. Pillsbury was and is a corporation engaged in commerce, as "commerce" is defined in the Clayton Act.

3. Fox was a corporation engaged in commerce, as "commerce" is defined in the Clayton Act, when it was acquired by Pillsbury.

4. The appropriate line of commerce — product market — to be considered in judging the legality of the acquisition of Fox by Pillsbury is frozen prepared pizza.

5. The appropriate section of the country — geographic market — in which the competitive effects of the acquisition are to be examined is the United States as a whole. [63]

6. The effects of the acquisition of Fox by Pillsbury were, or probably will be, that:

(a) Fox was eliminated as a competitor in the frozen prepared pizza industry;

(b) Concentration in the frozen prepared pizza market has been increased because one competitive entity has been combined with another;

(c) The competitive position of Pillsbury vis-a-vis its competitors in the frozen prepared pizza has been improved; and

(d) enhancement of Pillsbury's competitive vigor probably will result in a substantial increase in competition in various sections of the country in which Pillsbury did not compete previously in the frozen prepared pizza industry.

7. Fox was not a "failing company" in the sense in which that term is used in connection with Section 7 but the evidence as to its precarious financial condition coupled with the insignificance of the competition it offered and was likely to offer in the frozen prepared pizza industry rebuts the prima facie proof of violation which complaint counsel's presentation established.

8. The complaint should be, and hereby is, dismissed.

Dissenting Opinion of Commissioner Dixon

I agree entirely with the first six sections of the Commission's opinion but I cannot join its conclusion that this merger is unlikely substantially to lessen competition in the national market for frozen prepared pizza.

The merger combined firms with approximately 15% and 2% of the national market.[1] This occurred in an industry in which concentration has been increasing at an alarming rate. In the three

[1] Several sets of market share figures were cited by the ALJ. Those that appear most reliable were prepared by Selling Areas Marketing, Inc., (SAMI), I.D. 78-99, and will be cited herein. Pillsbury's market share in 1976 was 15.4% and Fox's was 1.7% Fox's share of the market had declined from 2.4% in 1975. This may have been due in significant part to its move to new production facilities in Joplin, Missouri, in which it encountered start-up problems and was only producing at 50-80% of capacity in March, 1976. (CX 49) Thus, I believe that "approximately 2%" is a reasonable characterization of its market share, and I certainly see no warrant for

(Continued)

years preceding the merger, the top three firms increased their market shares from 39.65% to 53.37%, while [2] 7-firm concentration rose 10 points from 70.74% to 80.74%. (I.D. 106) Respondent's Vice President of Mergers and Acquisitions projected that the top three companies will capture 60–70% of the national market by 1980. (Tr. 175)

As the Supreme Court has told us, it is the basic premise of Section 7 of the Clayton Act that competition will be most vital "when there are many sellers, none of which has any significant market share." *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 363 (1963). It may well be that in the market we deal with here, preservation of many small sellers, or even prevention of a tight oligopoly, is impossible, but I think that it is the purpose of the antitrust laws to ensure that at least the attempt is made.

While Fox's competitive vigor may well not have been on the order of that displayed by those companies of even smaller market share whose acquisition was condemned in *United States* v. *Aluminum Co. of America,* 377 U.S. 271 (1964) and *Stanley Works* v. *FTC,* 469 F.2d 498 (2d Cir. 1972), *cert. denied,* 412 U.S. 928 (1973), neither can I conclude that Fox was quite the competitive cipher that the majority describes. For many years Fox was a thriving, growing vendor of frozen pizza, with sales concentrated in a number of metropolitan areas in the Midwest and South. (I.D. 133-34) The company never failed to realize a profit, and as late as the September preceding its November acquisition it showed earnings of $43,000. In the year prior to the merger, Fox sold over $7 million worth of pizza, which gave it 2.4% of the national market. In 1976 it moved to different quarters, a non-recurring factor that may have contributed to its decline in market share to 1.7%. But neither the 1975 nor 1976 figures for the *national* market adequately account for Fox's competitive significance, because Fox's sales were limited to only certain areas of the country, in some of which it was in head to head competition with Pillsbury.[2] [3] The record is clear that in those areas of the country in which Fox did compete, it sold to such leading

characterizing Fox's share as a "declining 1.7%" when the decline *to* 1.7% may very possibly have been due in significant measure to non-recurring factors.

[2] Fox made 44% of its retail sales of frozen prepared pizza, exclusive of private label sales, in only nine metropolitan areas in the South and Midwest, during 1975–76, and Pillsbury made 25% of its total sales in those same areas during the same period. These nine areas accounted for only 16% of national pizza consumption. Fox's share in those areas ranged from 2% to more than 16% in 1975. (CX 36 *in camera*)

I agree with the Commission's finding of a national market, and with its conclusion that the record generated in this case will not support delineation of any particular regional submarket. However, not all pizza manufacturers sell in all marketing areas, nor would it be realistic for many to do so. For example, even an industry leader like Pillsbury has not entered the trade areas of New England, New York, and Los Angeles, due to insufficient production capacity. (I.D. 130) Retailers in these trade areas, then, could not realistically turn to Pillsbury in the event that they perceived wholesale prices to be getting out of line, unless perhaps prices became so distorted that Pillsbury was willing to reorient its marketing efforts. The situation with smaller producers is

(Continued)

retail food chains as Kroger and Winn-Dixie, and was regarded by leading frozen pizza producers as a "substantial competitor." (I.D. 109)

Under these circumstances, in a highly concentrated market hell-bent toward further concentration, I believe that the antitrust laws should be read to preclude the combination of one of the industry's leading firms with one of its smaller but nevertheless "substantial" competitors. As the Second Circuit Court of Appeals noted in *Stanley Works* v. *FTC, supra,* involving the joinder of an industry leader with a firm with 1% of a market in which 4-firm concentration was 49–51% (vs. roughly 60% here) and there was no comparable record evidence of increasing concentration:

> . . . though a market may be concentrated, forces may operate so as to maintain some level of competition and thus preserve the possibility of eventual deconcentration. That is why the continued independence of companies with relatively small market shares is so crucial to the health and vitality of a market threatening to become oligopolistic. 468 F.2d at 508.

Of course, one does not know how long Fox might have stood alone, but if precluded from selling out to an industry [4] leader, we may surmise that it would have combined either with a smaller industry member, or sold out to an outsider seeking to enter, either of which results would have been competitively preferable to the one that actually occurred.

The Commission, mindful of these considerations, finds that "there is no reason to believe that Fox, if acquired by a company outside the market, could have constituted a springboard to permit a new entrant to challenge the market leaders," and further, that barriers to entry were so low anyway that a potential entrant might do just as well by attempting *de novo* entry as by acquiring Fox. I find both these assertions to be unproven on the record, and I believe that it is respondent's burden to prove them if it wishes to consummate a horizontal merger of more than *de minimis* proportions in an industry as highly concentrated and with so pronounced a trend toward concentration as this one.[3]

even more pronounced in this respect. For these reasons I believe that it is proper to qualify the national market figures with some consideration of local marketing areas in which the merging parties competed, and doing so leads to the conclusion that the national figures understate the overall significance of this merger.

[3] This is also the position of the Department of Justice Merger Guidelines, of which this merger is in plain violation. Guideline 7 provides that the Department will ordinarily challenge a merger in any market, "not wholly unconcentrated" (which certainly characterizes 4-firm concentration of 60%) in which the aggregate market share of any grouping of the two to eight largest firms has risen by 7% or more during a five to ten year period preceding the merger (here 3-firm concentration rose by 13% in only *3* years), and which involves the acquisition by any firm in the relevant grouping of two to eight firms of any other firm whose market shares amounts to "approximately 2% or more." 1 Trade Reg. Rep. ¶4510 at 6884 (1971). I have earlier explained why I believe that "approximately 2%" is an abundantly fair characterization of Fox's market share. In all other respects, the characteristics of this industry far exceed those required to trigger prosecutorial action by the Department of Justice.

While one witness did testify that he had entered on the local level with an investment of only $50,000, it is plain from the record that entry on a nationwide or regional basis is a considerably harder proposition, and is becoming ever more so. In addition to capital costs (examples of which were $15 million to build a new plant for Pillsbury, down to $3 million paid by Purex to lease and improve its facility, I.D. 147) the ALJ found that considerable advertising and promotional expenditures are required to gain distribution of frozen prepared pizza, and a company must be prepared to sustain losses over an extended interval before effecting successful entry. (I.D. 148–50) While Fox was not a heavily advertised name brand, it obviously did have [5] considerable retailer recognition and entree into many important local marketing areas. For these reasons, I cannot conclude that Fox's assets would have proven altogether unattractive (or of no advantage over *de novo* entry) to a well-endowed potential entrant in search of a means of entering the frozen prepared pizza market.[4]

Of course, my surmise may be wrong, as may be that of the majority. The question, however, is who should bear the burden of proof in a case such as this. In my view, where concentration is as high, and increasing as rapidly, as it is here, a horizontal acquisition of more than *de minimis* proportions by a leading industry member should be presumed unlawful unless shown to the contrary.[5]

The Commission decision appears to rest importantly upon the fact that, in absolute terms, Fox was a very small company. I agree that this is an important concern in two respects. First, the absolute size of a company may be probative of its potential competitive ability. Secondly, and this appears to be a consideration upon which the majority's opinion turns heavily, there may be a countervailing competitive value in facilitating the ability of small companies to sell out, because ease of exit is an encouragement to entry by small entrepreneurs, and that is a competitive good. I share these concerns, but the problem is how to balance a global competitive consideration such as "encouraging entry by small entrepreneurs"

[4] I also find it interesting that in an industry in which entry barriers are assertedly so low, concentration should be increasing so quickly. Low entry barriers imply low scale economies — *i.e.* a firm with only a small market share can sell profitably at the same price as a firm with a larger market share. Why, then, do smaller firms seem to be uniformly losing out to larger ones? One reason may be, as the Commission itself has previously recognized, that increased concentration and the necessity to do battle with deep-pocketed competitors, may themselves be formidable barriers to entering or remaining in an industry. Cf. *Fruehauf, Inc.*, 91 F.T.C. 132, 220 (1978), appeal pending.

[5] This merger is clearly not of *de minimis* proportions. In *Stanley Works* v. *FTC, supra*, the Second Circuit sustained a Commission finding that the loss as an independent competitor of a company with a 1% market share, consisting of less than $900,000 in sales yearly, constituted a substantial lessening of competition. 469 F.2d 498, 501 n.7.

against the potential loss of competition from the acquisition of one of these small entrepreneurs in a particular market. [6]

I certainly agree, as the Commission states, that it is desirable that "owners of very small businesses with slight competitive potential have some reasonable flexibility to sell out." (Op. p. 19) I even agree that owners of very small businesses with not insubstantial competitive potential, like Fox, should have some reasonable flexibility to sell out if they tire of the competitive whirl. I do not agree, however, that such "reasonable flexibility" must include an absolute right to sell to a leading horizontal competitor in a very concentrated industry in which concentration is increasing. At a minimum, the Commission should insist under such circumstances that reasonable good faith efforts be made by the very small competitor to sell to someone other than a leading industry member before sale to the industry leader is condoned. Here, of course, as the majority acknowledges, (Op., p. 10) we have no evidence that any such reasonable efforts were made. If such reasonable efforts are not required, then we may predict that very small competitors will invariably seek to sell to industry leaders, because it is they who are most likely to be willing to pay a premium for the ability to snuff out a pesky opponent and acquire its share of the market. In the industry involved here, the likelihood of this occurrence is a matter of record. The president of one leading firm testified that Pillsbury's acquisition of Fox inspired his firm to consider a similar acquisition of a small competitor (a peculiar reaction if Fox's competitive value is as slight as the Commission imagines) though consummation awaits disposition of these proceedings. (I.D. 108)

The Commission purports to read the *General Dynamics* and failing company defenses narrowly, but its holding in essence applies a more lenient version of these defenses to the case of a very small acquired firm. If liability is made to hinge upon proof (by which side we are not told) of (1) entry barriers; (2) whether a company lacks "any special competitive potential"; and (3) whether there is "reason to believe that the acquired company, in other hands, would have been a vehicle leading to less concentration or more competition," then I cannot see how proof under the Commission's new "line of legality" will differ from proof under the old lines drawn by the courts. I do not mean by this to imply criticism of the Commission's approach — I quarrel only with the implication that it will make life any easier, or less remunerative, for the antitrust bar. Cases on the borderline of illegality inevitably involve difficult judgments. I agree that very small companies should be treated gently when they seek to exit, and I agree that the factors [7] considered by the Commission

(Op. p. 21) are important ones. I would simply add, however, that if the purpose of favoring small company mergers is to facilitate exit and thereby encourage entry, we should insist before condoning such mergers where they might otherwise violate the antitrust laws that a demonstration be made that there have been reasonable, good faith efforts to sell to someone other than a leading horizontal competitor.

Fox Deluxe Foods ranked ninth in the frozen prepared pizza market when it was acquired. Under the Commission's rationale, it is not clear how we can possibly object if the top eight firms in this market should now proceed to divide among themselves all the rest, since the top eight firms already control 85.52% of the market (I.D. 105), and could absorb the other 14% by means of each acquiring the 2% to which the Commission's decision entitles it. Competition in the sale of frozen prepared pizzas may now be (as it usually is in the estimation of industry members) "tough". I daresay, however, that when, in a few years, the firms that remain in this industry wake up to find themselves facing only seven competitors nationwide and far fewer that that number in any given local marketing area, they will discover, with no offense to the antitrust laws, a far more lucrative way of pricing their pizza than they have utilized to date. Perhaps this occurrence cannot be prevented, but I had always thought that the Clayton Act was designed to allow the government to try. As I read the record before us I would find that the challenged merger violates the law.

Concurring Opinion of Chairman Pertschuk

I concur in the Commission's determination that the acquisition of Fox by Pillsbury does not violate Section 7 of the Clayton Act or Section 5 of the FTC Act. For the reasons enumerated in the Commission's opinion, relating to the size and market share of the acquired firm and its lack of any special competitive potential, the absence of significant entry barriers, and other factors, this merger is not likely to have significant anticompetitive effects in the national market for retail frozen prepared pizza. I wish only to add my view that the formulation of any general rule of broad application out of the particular set of facts in this case would be a difficult and speculative task indeed.

Further, while I agree that preserving exit opportunities for very small firms can be procompetitive insofar as it indirectly lessens entry barriers, I believe that this consideration will influence the ultimate determination of a horizontal merger's lawfulness in only a very limited set of circumstances. I do not read the Commission's opinion to hold otherwise.

Opinion of the Commission

By Pitofsky, *Commissioner:*

I. Introduction.

This is a merger case involving an acquisition by the Pillsbury Company ("Pillsbury"), a leading manufacturer and marketer of a wide range of food products, including frozen prepared pizza, of Fox Deluxe Foods, Inc. ("Fox"), a rather small company with assets devoted in large part to the production and sale of frozen pizza. As will emerge below, Pillsbury-Fox was clearly a horizontal merger and resolution of the question whether that merger is illegal raises important questions about the location of the "bottom line" beneath which even horizontal mergers will be found not to violate Section 7. At issue are interrelated policy questions involving the "failing company" defense, the increasingly popular *"General Dynamics"* defense, and the definition of insubstantial anticompetitive effects under Section 7.

The complaint issued in this case in November 1976 charging that the merger between Pillsbury and Fox would substantially lessen competition in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5(a)(1) of the Federal Trade Commission Act, 15 U.S.C. 45. On November 15, 1976, the respondents stipulated to a [2] Preliminary Injunction which permitted the merger to be consummated, subject to certain conditions.[1]

The administrative law judge ("ALJ") dismissed the complaint. He found that a relevant market in which to assess the effects of this transaction was the retail sale of frozen prepared pizza in the United States. He further found, based on statistics prepared by Selling Areas Marketing, Inc. ("SAMI"), the four-firm concentration in the relevant market to be 60.8%, and that in 1976, the year of the acquisition, Pillsbury ranked third in the national retail frozen prepared pizza industry with 15.4% of sales, and Fox ranked eleventh with 1.7% of sales. (I.D. 104, 105)[2]

After finding that Pillsbury and Fox were horizontal competitors, the ALJ went on to reject the "failing company" defense proffered by respondents and deferred ruling on their contention that the proceeding was not in the public interest, stating that "the Commis-

[1] The complaint was amended to reflect the fact that the acquisition had been completed.

[2] The following abbreviations are used herein:

I.D.	- Initial Decision Finding No.
I.D. p.	- Initial Decision Page No.
CX	- Complaint Counsel Exhibit No.
RX	- Respondent Exhibit No.
Tr.	- Trial Transcript Page No.

sion has said that question is reserved to itself." (I.D. p. 57) Nevertheless, the ALJ relied upon Fox's "precarious position" (I.D. p. 57) as establishing a "*General Dynamics*" defense — that is, a defense based in his view, on the opinion in *U.S.* v. *General Dynamics,* 415 U.S. 486 (1973), in combination with *U.S.* v. *International Harvester Company,* 564 F.2d 769 (7th Cir. 1977). The ALJ dismissed the complaint, noting the following:

> Fox was not a "failing company" in the sense in which that term is used in connection with Section 7 but the evidence as to its precarious financial condition coupled with the insignificance of the competition it offered and was likely to offer in the frozen prepared pizza industry rebuts the prima facie proof of violation which complaint counsel's presentation established. (I.D. p. 63)

We affirm the dismissal of the complaint but on significantly different grounds. Our own review of the issues follows: [3]

II. The Industry.

There is general agreement among the parties, and the record supports the view, that the retail frozen prepared pizza industry has been undergoing substantial change. While most present manufacturers began as very small operations, often originating with a small pizzeria, brands are now developed for immediate nationwide distribution. Sales of frozen pizza grew from $407 million in 1975 to $463 million in 1976. (I.D. 102) Spurred largely by the recent entry — both by acquisition and by internal expansion — of national firms of substantial size,[3] the focus of competitive activity has shifted into intensive advertising and promotion.

Small manufacturers nevertheless remain viable. Market leaders differ regionally and locally, and private labelling has increased. Given the cost of plant, equipment, and the necessary advertising and promotional expenditures, it could take several million dollars to enter the retail frozen prepared pizza market on a nationwide scale. On the other hand, one pizza manufacturer testified that it was possible to enter the business on a local scale with a total investment of only about $50,000. (I.D. 151)

III. The Merging Parties: Pillsbury and Fox.

Pillsbury manufactures and markets a wide range of food products and is among the 200 largest U.S. corporations. (I.D. 4, 5) It entered the frozen prepared pizza business by its November, 1975 acquisition

[3] Pillsbury itself entered the industry by acquiring Totino's in 1975. General Mills acquired Saluto's in 1976, Purex acquired Ellio's in 1971, and Quaker Oats entered through its 1969 acquisition of Celeste. Large companies that entered *de novo* by developing their own product include Pet, Inc. Ore-Ida (Heinz), Fairmont Foods, and Stouffers. (I.D. 114).

of Totino's Finer Foods, Inc. Totino's gross sales of frozen prepared pizza for the twelve months ending October 31, 1975 were approximately $39 million (I.D. 6), and it ranked third in the industry with 13.7% of national sales. (I.D. 100)

Prior to its acquisition by Pillsbury, Fox was a family-owned Illinois corporation headquartered in Chicago. Until 1975, it was a profitable enterprise. Its sales increased from $6.4 million in 1972 to $11.2 million in 1975; over the same period its net worth increased 50%. (I.D. 18) However, one of Fox's two operating divisions, the Hotel and Restaurant ("H&R") Division, after showing profits through 1972, ran losses each year thereafter. The H&R Division was in the business of processing and selling various food products — primarily poultry — to food service customers such as [4] hotels, fast-food carryouts, hospitals, restaurants and the like. In February 1975, Fox's Board of Directors determined that a final decision on the fate of the H&R Division had to be made within six months. (CX 47)

Fox's Country Kitchen Division made and sold frozen prepared pizza, and was responsible for Fox's overall profitability through 1975. Fox's pizza sales in 1974 increased 20% over its 1973 sales. (CX 47) Although in 1975 Fox had freezer problems at its pizza plant in Carthage, Missouri, which necessitated the once-only expenditure of $350,000 over the course of approximately twelve months (Tr. 2409), and despite an unusually warm autumn that year which adversely affected frozen pizza sales (I.D. 30), Fox's pizza division remained profitable through 1975.

The Fox-produced frozen pizza had some reputation in the industry as a "price" or "in-and-out" brand (Tr. 1063), selling on the strength of low prices and numerous discount promotions. Fox did not engage in extensive advertising. (I.D. 11)

Although Fox took no effective action to initiate acquisition discussions, it was approached during 1975 by two companies to discuss a possible acquisition. The Peavey Company initiated contact with Fox, on the recommendation of a merger consultant. (Tr. 2595) Fox ultimately was not considered a suitable target for Peavey since Fox's line was positioned in the low-price, low-quality segment of the market, which made it incompatible with Peavey's other products. (I.D. 16) Peavey also doubted Fox's management strength and, based on a description of what was to be Fox's new plant, doubted that it "would be a plum." (Tr. 2600)

Early in January, Joe Fox met with a Vice-President of the Anderson-Clayton Company, a Houston-based food and food-related producer and distributor. (I.D. 17) The meeting was set up in response to a letter from Anderson-Clayton inquiring about Fox's interest in being purchased. (Tr. 2855) No follow-up visit or visit to Fox's Carthage plant was ever arranged.

At the end of 1975, Fox's Board of Directors decided to move its pizza operation from Carthage to a new plant in Joplin, Missouri. Fox applied to the Harris Trust and Savings Bank ("Harris"), with whom the company had banked since 1953, for a loan to finance the move. A $300,000 unsecured revolving loan — a line of credit — was approved. Harris had witnessed a "dramatic turnaround" in Fox's fortunes from 1972 to 1975, due to the success of the pizza division. (RX 48) Consequently, the short-term line of credit was extended despite its intended use to finance long-term [5] assets, on the assumption that it could be paid off easily with the proceeds of the anticipated liquidation of the H&R Division. (I.D. 18) Negotiations with Bon Ton Poultry Products, Inc. ("Bon Ton") for the sale of that Division were underway at the time.

Fox encountered a series of business misfortunes and adversities in 1976, but they were never so severe as to turn its pizza division into a failing operation. Fox's move to Joplin at the beginning of the year encountered start-up troubles. By March, production was only 50 to 80 percent of capacity (CX 49), and some of the equipment, much of which had been moved from Carthage, was causing problems. (I.D. 24) Nevertheless, Fox's Board of Directors was told that the quality of the product was "greatly improved in the Joplin plant" and production costs "were already lower". (CX 49) In light of the start-up problems and delays in the sale of Fox's H&R Division, Harris extended the outstanding line of credit for ninety days.

Things got no better as the year progressed. Sales were running twenty percent below projections, most of the losses due to increases in "controllable costs" (RX 16) which, unfortunately, were not being controlled. In May, Harris approved a temporary $50,000 "excess" to tide Fox over, due and payable at the end of June with the $300,000 already outstanding. (I.D. 22) The H&R Division continued to generate losses, draining needed capital from the pizza division. (RX 16) It was about this time, with its business prospects gloomy and other prospective buyers out of the picture, that Fox was first made aware of Pillsbury's interest in acquiring Fox's pizza manufacturing assets.

In June, the new Joplin plant was given a "4", the highest rating by inspectors from the U.S. Department of Agriculture. While problems remained,[4] Fox had agreed to take curative measures, and

[4] The plant was never wholly rodent-proofed, the meat room floor was deteriorating, the cooker leaked, the oven was hard to clean and caused fires of pizza crusts, and there was peeling paint in the sauce and meat rooms. (I.D. 15)

in any event the problems had "never caused an unsanitary, unwholesome or adulterated product to be produced at the Joplin facility." (CX 76) Estimates of the amount of investment required to bring the Joplin plant into full and non-temporary compliance with U.S.D.A. requirements varied, but none predicted that the [6] necessary amounts would be beyond Fox's current financial capacity.[5] Shortly thereafter, Harris increased Fox's unsecured line of credit from $350,000 to $500,000 for an additional ninety days, by the end of which time it was understood that either the H&R Division would be sold, all of Fox would be sold, or Harris would secure its loan and set up a repayment program. (I.D. 25) On July 22, 1976, Pillsbury's Vice-President of Mergers and Acquisitions, made a verbal offer to purchase Fox. (CX 46-23; CX 51)

At the Board of Directors meeting in August, Joe Fox reported on Pillsbury's offer of approximately fourteen dollars worth of restricted Pillsbury common stock for each outstanding Fox share. The Board rejected the offer as insufficient, but remained interested. The Board also voted to reject, without continued interest, the latest offer by Bon Ton for Fox's H&R Division.[6] (CX 51)

The pizza operation showed a profit in September, 1976 of $43,000. (CX 67) The H&R Division had not been sold, and an influx of capital was still needed to bring the Joplin plant to top efficiency. A memo from Fox's Vice President for Operations to its President outlined $280,000 worth of items which would be necessary if the Joplin plant were to meet all government requirements, provide product safety, improve case costs, provide employee safety, maintain the current level of performance, and improve the quality of the product. (RX 15)

The pizza division of Fox remained profitable throughout the fall of 1976. According to Mr. Horsch, president of a venture capital firm who testified as an expert witness on behalf of Pillsbury, "[t]he average profitability [of the pizza division] in the three months prior to the acquisition, which were the significant profitable months, was about thirty thousand dollars a month." (Tr. 2721)

Pillsbury acquired Fox on or about November 15, 1976, paying $3 million in Pillsbury common stock. On the same day it acquired Fox, Pillsbury sold the H&R Division to Bon Ton, for $174,500 in cash and $80,183 in notes. (CX 74) Pillsbury had also acquired the H&R Division's $365,000 worth of accounts receivable, and collected

[5] The Fox Board of Directors voted on June 14, 1976 to spend $61,820 to upgrade the plant. (CX 50) A June 3, 1976 memo to the Chairman of the Board from Fox's President Boyce, and Vice President of Operations, Balster, had estimated that only $36,000 would be necessary to solve all the problems noted by the U.S.D.A. inspectors. (Tr. 2408)

[6] At issue was the manner by which the H&R Division's accounts receivable could be collected. (I.D. 27) Fox wanted Bon Ton to take steps culminating in the placement of customers on a C.O.D. basis at Fox's direction if they failed to pay within a stated time. Bon Ton refused. The Fox Board voted to terminate the negotiations.

$307,000 against those receivables within a few months. (Tr. 2889) Pillsbury also turned out to have acquired $272,000 worth of signed but unmailed checks to various suppliers of both divisions of Fox, for the payment of which Pillsbury advanced $130,000. (Tr. 2888) Taking their assets and debts into account, the total acquisition price was approximately $3,156,000.

IV. Relevant Markets.

The parties agree that the United States is a relevant section of the country. Complaint counsel also suggest — and respondents dispute — that there are various regions, which correspond more or less to the greater metropolitan areas SAMI uses as bases for its statistics, which also constitute relevant geographic submarkets for the assessment of the effects of this merger.

There is considerable evidence that retail frozen pizza manufacturers often target, or even confine, their marketing regionally. Thus, in any particular city, only Pillsbury, Fox, and three or four other frozen pizza manufacturers might be selling at any given time. In such local markets Pillsbury's and Fox's market shares of course would be high and perhaps sufficient to indicate anticompetitive effects under Section 7. But "[w]e do not believe the pie will slice so thinly," *Tampa Electric Co.* v. *Nashville Coal Co.*, 365 U.S. 320, 331 (1961), at least not on this record. The test for measuring geographic market is where consumers (in this case retailers) can practicably turn for an alternative source of supply. *Tampa Electric Co., supra,* 365 U.S. at 327; *U.S.* v. *Grinnell Corp.*, 384 U.S. 563, 588 (1966) (Fortas, J., dissenting). *See also U.S.* v. *Philadelphia National Bank,* 374 U.S. 321, 357-9 (1963). Here the record is clear that frozen pizza manufacturers could sell virtually throughout the United States from a single plant with no significant cost disadvantages.[7] (I.D. 125-128, 131) Thus, the power [8] of any given group of sellers serving a city or region at a given time to raise price is limited by the capacity of virtually all other domestic manufacturers to compete on practically an equal footing in that city or region — an economic situation which requires a finding of a national market and the elimination of geographic submarkets.[8]

Respondent contests the ALJ's finding that retail frozen prepared pizza is a relevant product market, arguing that the market is too narrowly defined. Respondent contends, first, that all forms of pizza

[7] The fact that transportation costs pose no significant barriers to distribution to remote customers is evidenced by the finding that "[e]ven a small manufacturer like 'Tree Tavern' " from New Jersey can ship to Puerto Rico and the U.S. Virgin Islands. (I.D. 125)

[8] Even under these circumstances, of course, special factors, like slight economic barriers, could produce submarkets. However, the record in this case contains no evidence on which to base such findings.

— including dry mix pizza, refrigerated pizza, grocery shelf-stable pizza, restaurant pizza, and pizzeria pizza — must be included in the market, basically because "they are functionally interchangeable for the purpose for which they are made." (Respondent's Answering Brief, p. 31) Other frozen foods are also claimed to be effectively competitive, since frozen prepared pizza must vie with those products for space in the grocer's freezer chest. We think respondent describes an unduly wide competitive arena.

To find his way along the imprecise route toward product market definition, the ALJ turned to the familiar guideposts of *Brown Shoe Co.* v. *U.S.,* 370 U.S. 294 (1962). He found that retail frozen prepared pizza exhibited a number of characteristics, sufficient to identify it as a separate line of commerce (I.D. p. 43): unique characteristics of pizza preparation (the use of preservatives and blastfreezing); the fact that those companies which manufacture frozen prepared pizza (or the divisions of companies which do) make only that food product; industry recognition of separateness through manufacturers' perceptions and the existence of a trade association; and, most significant, a lack of price sensitivity between retail frozen prepared pizza and other pizzas or frozen foods.[9] We think these factors are adequate to support a finding that retail frozen prepared pizza is the proper product market in this case. [9]

V. "Failing Company"

Assuming a relevant market consisting of sales of frozen pizza throughout the United States, we would have a merger where, as the ALJ found, the acquiring company, Pillsbury, accounted for 15.4% while the acquired company, Fox, accounted for 1.7%. Respondent contends that regardless of these market shares and other aspects of customary analysis of the anticompetitive effects of mergers, this acquisition should be found legal because Fox was a "failing company." The burden of proving such a defense falls, of course, "on those who seek refuge under it." *Citizen Publishing Co.* v. *U.S.,* 394 U.S. 131, 138-9 (1969). We agree with the ALJ that Pillsbury has failed to discharge its burden of proof.

The Supreme Court, in two merger cases,[10] set out the factual predicate which must be present for a company to be "failing" in a

[9] Respondent argues that such broad price sensitivity between pizza and other foods exists. (Respondent Proposed Finding of Fact 64) As support, it cites the testimony of a grocer that when meat prices rose in 1973 and 1974, sales of meat went down and sales of frozen pizza rose correspondingly. We are not sure what the import of this information is since we do not understand respondent to argue that "meat" and frozen prepared pizza are in the same market. In any event, this testimony tells us little since it does not specify the amount of increase in meat prices, or the extent of responding increases in pizza sales.

[10] *International Shoe Company* v. *F.T.C.,* 280 U.S. 234 (1930), and *Citizen Publishing Company* v. *U.S.,* 394 U.S. 131 (1969).

way that its acquisition, regardless of competitive consequences, does not offend the antitrust laws. First, the company must be in such poor competitive condition that "the only alternatives presented are involuntary liquidation, insolvency, or outright sale."[11] It is only at this point in a company's life that the advantage of preservation of the company as a "unit in the competitive system"[12] is overcome by the "seriously injurious consequences otherwise probable"[13] likely to befall the company's employees, creditors and shareholders.[14]

Second, there must have been a good faith effort to determine whether there were other purchasers available whose acquisition of the company would have resulted in less anticompetitive effects.[15] This combines with the critical financial state of the company to make the "failing company" defense a truly "last straw" doctrine. [10]

These descriptions of the essential predicate paint a different picture from the one we have of Fox prior to the acquisition. Fox' total operation probably was losing money in 1976, and the company's total debt had increased and its working capital was depleted. But it had made money in previous years, had a solid and continuing source of credit, and was not on the brink of bankruptcy. Fox recognized all along that its H&R Division had to be sold or liquidated for it to be on sound financial footing over the long term. Of course, Pillsbury did just that as soon as it acquired Fox. Had Fox done this (instead of rejecting an offer to buy the H&R Division in August, 1976) the record indicates that its pizza operation, standing alone, would have been profitable in 1976, the company's worst year. But the financial straits of the H&R Division amounted to neither the imminence of financial ruin nor even "the probability that bankruptcy will ensue."[16] The need to convert one division which, though concedely generating losses, is being kept afloat by another, profitable division, into available capital[17] hardly places a company on the same footing as one facing the virtually immediate advent of receivership.

As to the requirement that Fox make good faith efforts to seek a less anticompetitive alternative, the most we can say about other

[11] *International Shoe, supra,* 280 U.S. at 302.

[12] *Citizen Publishing, supra,* 394 U.S. at 138.

[13] *International Shoe, supra,* 280 U.S. at 302.

[14] *See* Bok, "Section 7 of the Clayton Act and the Merging of Law and Economics", 74 Harv. L. Rev. 226, 340–1 (1960). Only where the sole alternative is the complete discontinuance of the company does an adverse effect on competition due to merger become the "lesser of two evils." *U.S.* v. *General Dynamics Corp.,* 415 U.S. 486, 507 (1974).

[15] *Citizens Publishing, supra* 394 U.S. at 138.

[16] S. Rep. No. 1775, 81st Cong., 2d Sess. 7 (1950).

[17] Pillsbury had no trouble in both selling the H&R Division to the party with whom Fox had negotiated, and overcoming the collection problem at which Fox had balked.

prospective purchasers for Fox is that we don't know if there might have been any. The two companies other than Pillsbury who expressed interest in Fox both started and ended their contacts with Fox in 1975, several months before Pillsbury appeared on the scene. Both nibbles were instigated by the other companies, not Fox. The strongest argument respondents can put forward is that there was "no buyer on the horizon for the losing H&R Division" (Respondent's Answering Brief, p. 24), and that the company's overall prospects were so unpromising that it would have been unlikely that purchasers other than Pillsbury could have been found to acquire either the H&R Division or the entire company. (Respondent's Answering Brief, p. 25) But that simply is not adequate to satisfy the requirement under *Citizen Publishing* that a company contemplating sale make a good faith effort to find a purchaser whose acquisition would be consistent with the purpose of Section 7 to [11] preserve competition.[18] Here, there is nothing in the record to indicate that Fox did anything about seeking prospective acquirers other than to respond to Pillsbury's initiatives.

All in all, Fox's actions were not those of a company trying to avert the threat of total loss to its shareholders, creditors and employees by seeking out the best deal, one which sought reasonable offers most consistent with the purposes of Section 7. Fox remained passive while potential buyers sought it out, did not seek a long-term loan to master a series of temporary problems, and sat on an unprofitable operation which, had it been in dire straits, it could have liquidated. We conclude that while Fox faced serious financial problems, it did not satisfy the stringent standards that apply to a "failing company" defense.

VI. General Dynamics

Complaint Counsel appeals the ALJ's determination that evidence of Fox's weakened status as a competitor caused by its financial instability was sufficient to overcome Complaint Counsel's *prima facie* case. Respondent asserts that recent changes in the retail frozen pizza industry combined with Fox's weakness "from a production standpoint and in the marketplace" (Respondent's Answering Brief, p. 13) compel the conclusion that no substantial lessening of competition will result. The specific marketplace changes to which respondent points involve the entry of large

[18] *See also*, Department of Justice Merger Guidelines, ¶9 (1968), 1 Trade Reg. Rep. (CCH) ¶4510 at 6884, where the failing company defense requires that "good faith efforts by the failing firm have failed to elicit a reasonable offer of acquisition more consistent with the purposes of Section 7 by a firm which intends to keep the failing firm in the market."

national companies which have changed the focus of competition to one emphasizing advertising and heavy promotional activities. Respondent and the ALJ rely principally upon the Supreme Court's decision in *U.S.* v. *General Dynamics Corp.*, 415 U.S. 486 (1974), and a subsequent Court of Appeals case, *U.S.* v. *International Harvester Company*, 564 F.2d 769 (7th Cir. 1977). We do not agree that this case presents an appropriate application of what has come to be called the *"General Dynamics"* defense.

The scope of a proper *"General Dynamics"* defense raises the question of what kinds of evidence are relevant to explore the anticompetitive effects of a merger. In *Brown Shoe Co.* v. *U.S., supra,* the first and landmark exploration of Section 7 enforcement issues, the Court indicated that [12] a rather wide range of economic and other facts would have a bearing on the existence of a violation. But the steady course of decision thereafter demonstrated a recognition by the Court that merger enforcement would have to be streamlined, and key economic facts such as combined market shares relied on to a substantial degree, to permit effective enforcement. *U.S.* v. *Philadelphia National Bank, supra; Ford Motor Co.* v. *U.S.*, 405 U.S. 562 (1972). Continuation of this steady enforcement trend was thrown into doubt in *General Dynamics* where the Court rejected market share and concentration data as conclusive indicators of anticompetitive effect, finding in that case that a merger involving apparent market shares as high as 15.1 and 8.1%[19] did not constitute a violation of Section 7 when all facts about coal production and the changing nature of competition in that industry were taken into account. Since then, companies attempting to defend mergers have often argued (as have respondents in this case) that mergers involving percentage shares previously thought presumptively illegal or likely to produce a finding of anticompetitive effect under Section 7 in fact had no anticompetitive effect when "all the facts" were known. It is important, therefore, to examine exactly what the *General Dynamics* opinion did and did not mean in order to deal with respondents' contentions in this case.

In *General Dynamics,* the Government challenged a merger involving two coal producers, alleging that the proper market was the production and sale of coal in two midwestern areas. The District Court dismissed the complaint and the Supreme Court affirmed on the ground that, while the past production and current sales of the two companies were substantial, the "focus of competition"[20] in the coal industry was on the ability of producers to procure new long-

[19] 415 U.S. at 496.
[20] *Id.* at 501.

term supply contracts. Consequently, the Government's production statistics were of little use in measuring the acquired company's (United Electric's) future ability to compete, since such statistics represented only deliveries under outstanding contracts.[21] In fact, the Court said, the proper measure of competitive strength in the market was "the state of a company's uncommitted reserves of recoverable coal."[22] United Electric, fifth in production, was tenth [13] in reserve holdings, with less than 1% of the reserves held by producers in the larger geographic market alleged by the Government.[23] "Even more significantly", less than 8% of those reserves were uncommitted, and the Court specifically noted that United Electric had no prospect of acquiring new reserves.[24] Moreover, the evidence relied upon by the District Court "could not reflect a positive decision on the part of the merged companies"[25] to influence the competitive picture. The coal industry had changed. Consumption patterns had been altered by the availability of other energy sources. Most coal was purchased by electric utilities, and almost entirely by means of long-term requirements contracts. Such evidence "necessarily and logically implied that United Electric was not merely disinclined but unable to compete effectively".[26]

Finally, the Court distinguished the acquisition of United Electric from that of a "failing company".[27] United Electric would not have gone out of business but for the merger. It would have remained in the market, producing coal, and delivering on its outstanding contractual obligations. The question the Court addressed was rather what the effect of United Electric's continued presence in the market might be, decided that United Electric, without the ability to increase its reserves, had no power to substantially affect competition for new requirements contracts.

Properly viewed, all *General Dynamics* really concluded was that the government had been arguing for a measure of market share which inaccurately portrayed the competitive significance of the merger.[28] Changes in the competitive environment were a reason why reserves rather than past production or current sales were an accurate indicator [14] of market power, but the merger complaint

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[21] *Id.* at 501.
[22] *Id.* at 502.
[23] 415 U.S. at 502.
[24] *Id.* at 503.
[25] *Id.* at 506.
[26] *Id.* at 506.
[27] *Id.* at 507–8.
[28] *Cf. U.S.* v. *Amax, Inc.*, 402 F. Supp. 956, 971 (D. Conn. 1975), where the District Court enjoined a contemplated merger after determining that, given the focus of competition in the relevant market (the production of refined copper), the market shares of the merging companies as properly measured (by refining capacity) were such that the merger would substantially lessen competition.

was dismissed essentially because market shares, accurately measured, did not justify a finding of a substantial lessening of competition.

Viewed in that light, Pillsbury cannot validly assert a *"General Dynamics"* defense. None of the evidence presented here in any way undermines the utility of sales figures as a measure of market share or an accurate indicator of market power. Annual sales have been and seem likely to remain the "focus of competition" in the retail frozen prepared pizza industry. The recent entry of larger national companies who engage in intensive advertising and promotional campaigns has changed the industry, but it has not changed the gauge by which a company's market power should be measured. Pizza unlike coal is obviously not an exhaustible natural resource that either company had committed by contract or was in danger of depleting permanently. Small, regional and private label manufacturers remain viable and effective competitors; Fox itself never had any trouble selling as much pizza as it could make. And while competition at the national level may now exist that is beyond Fox's means, it does not follow that Fox at its level does not exert some price pressure on the market leaders. Thus, this is not a case in which market share statistics give "an inaccurate account of the acquisition's probable effect on competition."[29]

General Dynamics speaks to the care with which we must determine what factors to take into account to maximize the accuracy of our prediction of a company's ability to compete in the future. In this case, we think that market shares and concentration ratios are the "primary indicia" of competitive strength,[30] and the proper means to measure it.

Respondent contends that even if the market shares are an accurate measure of present competitive activity and even if Fox were not a "failing company", Fox's financial condition was so poor at the time of the acquisition that it should be considered a seriously weakened competitor in the future. In advancing that argument, respondent relies heavily on *International Harvester.*[31] That case involved Steiger [15] Tractor, Inc. ("Steiger") and International Harvester ("Harvester"), both of which manufactured four-wheel

[29] *Citizens & Southern National Bank, supra,* 422 U.S. at 120.

Retail frozen prepared pizza remains a market, like "groceries or beer" cited in *General Dynamics,* in which "statistics involving annual sales naturally indicate the power of each company to compete in the future." *General Dynamics, supra,* 415 U.S. at 501.

[30] *U.S.* v. *Continental Can Co.,* 378 U.S. 441, 458 (1964).

[31] *U.S.* v. *International Harvester Company,* 564 F.2d 769 (7th Cir. 1977).

drive farm tractors. Steiger supplied such machines to Harvester for resale and also sold them through dealers.[32] In April 1974, Steiger and Harvester entered into an agreement whereby Harvester acquired 39% of Steiger's common stock, and as a result received three directors on Steiger's nine-member Board. The Government challenged this agreement under Section 7; the District Court found for the defendant and the Court of Appeals affirmed.

Steiger's story from 1970 to 1974 is one of a feisty company whose financial outlook was extremely grave and which attempted energetically for several years to bring itself back to fiscal health and finally succeeded. Steiger showed losses in 1970 of over half a million dollars. It obtained bank financing in 1971 but only with the personal endorsement of its chairman, which it had to supplement with money from a venture capital firm. Both loans were called in early 1972 and Steiger turned for capital to customers, and finally to a factor (who charged almost twice the prime lending rate at the time). In 1973, Steiger's balance sheets showed an improvement, but the company was carrying a huge load of costly debt.

The purchase agreement provided that Harvester could in no way limit or control Steiger's business activities. The parties simultaneously executed a five-year Manufacturing Agreement, with Harvester obligated to buy a certain number of tractors assembled by Steiger through 1979.

The Court of Appeals, in upholding the transaction, relied principally on Steiger's precarious financial condition at the time of the agreement which "placed it at a competitive disadvantage,"[33] and which was cured by the influx of funds from Harvester.[34] Moreover, the court found that the [16] agreement had made Steiger a more aggressive, independent competitor, whose presence contributed to a marked decrease in concentration in the relevant markets, evidenced by "intensified price competition."[35] The Court read *General Dynamics* not to be limited to situations involving a depletable natural resource, nor even to situations where statistics concerning past sales are a misleading indicator of market power, but to extend to all cases where weakness, financial or otherwise, impairs a company's ability to compete.

[32] In 1973, Steiger manufactured four-wheel drive tractors for itself and others accounting for 19% of industry shipments; Harvester's own production represented 6%. The four-firm concentration ratio was 83%. Steiger also produced 7% of all high powered farm tractors while Harvester's production was 27%, and the four-firm concentration ratio in that market was 73%. 564 F.2d at 771.

[33] 564 F.2d at 776.

[34] The court rejected the notion that Harvester had to be shown to be the *only* source of financing because, i said, defendants did not rely on the failing company doctrine. 564 F.2d at 779. The Court added that there wa evidence that Harvester was indeed the only purchaser, but that was inferred from the "onerous options otherwis available to Steiger", not from any evidence that Steiger sought out other bids. 564 F.2d at 779.

[35] 564 F.2d at 778.

Inclusion of financial weakness as a separate factor or defense — other than in a failing company situation, of course — raises serious antitrust policy problems. First, there may be a sort of double counting in that financial weaknesses may already be reflected in a market share of the troubled company that is lower than it would have been but for the financial problems. Second, the issue of financial weakness is extremely difficult to handle in court, and susceptible to invented claims and vague expert testimony generating factual issues that the courts are not well equipped to measure. Third, if all sorts of company "weaknesses" or structural market changes operating to the disadvantage of particular companies, can overcome a *prima facie* case of illegality, then the whole valuable trend in merger enforcement toward streamlining cases by concentrating on properly measured market shares and concentration ratios will be undermined. This is not to say that in a close case, financial weakness cannot be taken into account along with many other factors in predicting the market consequences of a merger, but rather that there ought not be a broad *"General Dynamics"* defense that may be relied upon to overcome clear instances of illegality based on market shares and concentration ratios.

In addition, there is the issue of why the financially weak company, as a result of diminished market shares, should have an option to sell out to a competitor. If money problems are plaguing the firm, money can cure them and there seems no reason to believe that the money cannot be obtained from a variety of sources other than a competitor. While the court did find in *International Harvester* that Harvester was "the only practicable source," there was no evidence that Steiger had shopped around for another purchaser or source of funds which would have produced a less [17] anticompetitive result.[36] If Steiger's money troubles were so severe that its existence was in question, then, like any "failing company," it should have been required to seek out the least anticompetitive alternative purchaser. Certainly, there is little logic or fairness in imposing a rigorous requirement of search for a preferred purchaser on a 'failing company" on the brink of extinction and not on one that's nerely "troubled."

For all of the reasons cited above, we conclude that if *International 'arvester* reads *General Dynamics* to extend to a wide array of stances where "financial weakness" constitutes a defense for

[36] See note 34, *supra*, p. 15. Interestingly, in *General Dynamics, supra*, the Supreme Court particularly noted : it was only additional uncommitted reserves which could have restored the acquired company's potential as a petitor and that the company had "neither the possibility of acquiring. . .nor the ability to develop" those rves. 415 U.S. at 503.

otherwise clearly illegal mergers, we respectfully decline to follow it.[37]

The circumstances surrounding the "financial weakness" of Fox prior to its acquisition by Pillsbury are instructive in demonstrating why such factors ought not to lead to a finding of no violation of Section 7. Fox had serious financial difficulties, but there were reasons to believe they were temporary, and certainly they were susceptible to solutions other than sale to a horizontal competitor. Avenues of financial support other than its one line of credit were never explored. Other potential acquisition candidates were not canvassed prior to the acquisition by Pillsbury. Finally, Fox almost certainly could have solved its financial problems by selling off its H&R Division and eliminating the drain on its otherwise profitable pizza business — as Pillsbury in fact did immediately after completion of the merger. Thus, even if evidence of financial weakness were to constitute some sort of defense in Section 7 enforcement — an approach which we believe should rarely, if ever, be followed except in a "failing company" context — Fox's financial difficulties were not of a sort to justify such a defense.

VII. Absence of Significant Anticompetitive Effect.

Although Fox does not qualify as a "failing company" and is not entitled to any variation of the *"General Dynamics"* defense, we nevertheless find that the Pillsbury-Fox merger does not violate Section 7 because it is not likely to have significant anticompetitive effects. [18]

Pillsbury ranked third in 1976 with 15.4%.[38] Fox's share had decreased from 2.4% in 1975 to 1.7% in 1976. On a strict percentage basis, these market shares fall in the gray area at the edge of potential illegality under the Department of Justice guidelines for horizontal mergers,[39] but a finding of a violation would not be entirely unprecedented.[40] We note in addition, however, that while

[37] There is an alternative reading of *International Harvester* limiting it to its facts, *i.e.*, a partial stock acquisition which did not give the shareholder company control. Such reading would render *International Harvester* simply inapposite to this case.

[38] Respondent contested the market share figures used by the ALJ. Complaint counsel had argued that Pillsbury ranked second in 1976 with 18.28%, while respondents agreed to the No. 2 ranking but thought the market share was only 13.7%. Our disposition of this case would be the same whichever set of figures is used.

[39] Department of Justice, Merger Guidelines, ¶5, 6 and 7 (1968), 1 Trade Reg. Rep. ¶4510 at 6884 (1971).

[40] *Cf. U.S.* v. *Aluminum Co. of America*, 377 U.S. 271 (1964); *Stanley Works* v. *FTC*, 469 F.2d 478 (2d Cir. 1972). Of course, mergers have been found illegal where the combined market share was less than the 17.1% involved here. See *e.g., Beatrice Food Co.* v. *FTC*, F.2d 303 (7th Cir. 1976) (7.6 and 2.3%); *Liggett & Myers, Inc.* v. *FTC*, 567 F.2d 1273 (4 Cir. 1977) (10.99% and 4.4%). This case is different, however, because of the small size and insignificant competitive potential of the acquired company.

the four-firm concentration ratio for the national frozen pizza market was found by the ALJ to be 60.8%,[41] barriers to entry, even for fairly small companies, were moderate to low.

Fox was not only small but it was in no sense a company with special competitive potential which might lead to a conclusion that modest market shares understated the future competitive significance of the acquired company. Thus, in *U.S.* v. *Aluminum Co. of America,* 377 U.S. 271 (1964), the acquisition of a company accounting for only 1.3% of sales was nevertheless found illegal because it was an aggressive independent competitor, a pioneer in efficient research and sales, and possessed of special aptitudes and skills in the relevant product line. Here, Fox had been a price-oriented marketer, but there's no evidence that it was sufficiently aggressive to constitute a destabilizing price cutter in the market. [19]

As Commissioner Dixon rightly points out in his dissenting opinion, the Supreme Court has found that a trend to concentration can be an important factor in merger analysis, occasionally leading to a finding of illegality even when small horizontal acquisitions are involved. See *Brown Shoe Co.* v. *U.S., supra,* 370 U.S. at 345-6. Using figures most favorable to complaint counsel (*supra,* note 41), the four firm concentration ratio in retail frozen pizza sales increased from 55.48% in 1974 to 62% in 1976, and the seven firm concentration ratio increased from 70.74% in 1973 to 80.74% in 1976 — significant increases in concentration. In dealing with concentration trends, however, the courts have further stated that the underlying rationale for taking such trends into account involves the necessity of preserving the small firm as a vehicle for "eventual deconcentration" of the market. *Philadelphia National Bank, supra,* 374 U.S. at 365, n. 42; *cf. Stanley Works* v. *FTC, supra,* 468 F.2d at 508. Here, there is simply no reason to believe that Fox could have combined with other small frozen pizza manufacturers to challenge larger companies in the market. Also, given Fox's size and the nature of its assets, there is no reason to believe that Fox, if acquired by a company outside the market, could have constituted a springboard to permit a new entrant to challenge the market leaders. Despite a trend toward concentration in this industry, it is clear that *de novo* entry is feasible and has actually occurred.[42] Thus it would appear that an outsider could as easily achieve a significant market position through complete *de novo* entry as through the acquisition of Fox,

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[41] Various concentration ratios were introduced into evidence, depending on whether SAMI or Market Research Corporation of America data was used, ranging from a high of 4:62% in 1976 to a low of 4:49.3% in 1976. D. 100; CX 55, 60, 64.

[42] See note 3, *supra,* p. 3.

and, as a result, the importance of preserving Fox as an eventual deconcentrator fades.

There is no other reason to believe that Fox's declining 1.7% of national sales in 1976 does other than accurately portray its competitive significance. The fact that its entire assets were exchanged for approximately $3 million worth of common stock is some indication that no large premium was paid here by Pillsbury to eliminate a significant competitive factor.

Horizontal mergers have never been viewed as illegal *per se* under the antitrust laws even though a merger predictably will eliminate competition more completely than any price-fixing or other anticompetitive agreement.[43] Long-term competitive considerations require preservation of [20] ease of entry, and opportunity for businessmen to take entrepreneurial risks. The other side of that coin is a largely unarticulated policy, a clear corollary to the first, which would preserve exit opportunities where significant anticompetitive results do not occur. It is essential that the owners of very small businesses with slight competitive potential have some reasonable flexibility to sell out. This set of considerations is particularly compelling where the small acquired asset is a family-owned business which has come upon uncertain and perhaps adverse business conditions. Professor Areeda summarized relevant factors that attend that situation in the following terms:

> The retiring entrepreneur may lack confidence in his successors or may prefer the security of portfolio diversification. Or a firm may be impelled toward merger by the fact or fear of relative decline. The actual or prospective difficulties might be in management, research, marketing, capital, labor, or anything else that affects a firm's fortune. Sale of the company as a going business may cause minimum disruption to owners, managers, suppliers, customers, employees, and communities. To facilitate exit when it is desired may indeed facilitate entry. The likelihood of exit with minimum loss or maximum gain increases the attractiveness and reduces the risk of entering a market.[44]

Congress was similarly aware of the importance of designing antimerger legislation so as not to render unduly difficult market exit by very small firms. When Section 7 was amended to extend to asset as well as stock acquisitions in 1950[45] the question of the new

[43] *Cf. U.S.* v. *Socony-Vacuum Oil Co., Inc.,* 310 U.S. 150 (1940), which established a *per se* rule against "[a]ny combination which tampers with price structures." 310 U.S. at 221.

[44] Areeda, *Antitrust Analysis,* 2nd Ed., para. 617(h) at p. 690 (1974).

It is worth noting that this array of factors are some of the reasons why mergers among small companies, or acquisition by a large company of a very small company, should not be treated under *per se* rules or even found to violate Section 7. Citation of this variety of factors is not meant to suggest that each should properly be the subject of proof in a merger case.

[45] Pub. Law 899, 64 Stat. 1125; (1950).

statute's impact on the opportunity of small business to move in and out of a market was addressed: [21]

Furthermore, the Supreme Court and the Federal courts have not applied the present strict language of Section 7, even in cases of stock acquisition, so as to prevent a small corporation from selling its business *or* of merging with another small business. The Supreme Court has only applied the present language of Section 7, even in the case of stock acquisitions, to large transactions which would substantially lessen competition, or tend to create a monopoly. [emphasis added][46]

As noted earlier in this opinion, the law properly sets a demanding standard before a "failing company" defense can be asserted successfully, and we believe any additional relaxation in previous Section 7 enforcement approaches that may be thought to be generated by the *General Dynamics* decision be given a very limited scope. These narrow interpretations of two possible "exceptions" to general antitrust principles can be more fairly maintained if there is an appreciation that mergers between two small companies, or between a large and a very small company, do not necessarily violate Section 7. We believe it is better antitrust policy to delineate a fairly clear line beneath which mergers between horizontal competitors will not be declared illegal than to create vague and potentially sweeping exceptions likely to complicate and delay enforcement actions. We believe the following describes an acquisition that falls below that line: the acquisition by a non-dominant[47] company of a very small competitor (in absolute terms), lacking any special competitive potential and with a declining 1.7% market share, where there are no significant barriers to entry and when there is no reason to believe that the acquired company, in other hands, would have been a vehicle leading to less concentration or an increase in competition.

FINAL ORDER

This matter has been heard by the Commission upon the appeals of complaint counsel and respondent from the initial decision and upon briefs and oral argument in support of and in opposition to the

[46] H. Rep. No. 1191, 81st Cong., 1st Sess. 7 (1949). This point was also made repeatedly in the floor debates. *See, e.g.,* 96 Cong Rec. 16435 (1950) ("Any action by the Federal Trade Commission designed to halt mergers of an inconsequential nature would not be in accordance with the language of the bill and would not be upheld by the courts.") [Remarks of Sen. O'Conor]; 96 Cong. Rec. 16441 (1950); [Remarks of Sens. Kem and O'Conor]; 96 Cong. Rec. 16444 (1950) [Remarks of Sen. Kefauver].

[47] We have no occasion to define here all the circumstances in which an acquiring firm would be so large that acquisition of even such an insignificant competitive factor as is involved here might violate Section 7. An obvious example would be a situation in which the acquiring firm is a monopolist. Another example might involve a "dominant firm", sometimes defined to possess between 20 and 30% of a relevant market, *cf. Philadelphia National Bank, supra,* 374 U.S. at 364-5 n.41, and standing first or a very close second in that market.

appeals. For the reasons stated in the accompanying Opinion, the Commission has denied the appeals.

It is ordered, That pp. 1–50 of the initial decision of the administrative law judge be adopted as the Findings of Fact of the Commission, except insofar as they are inconsistent with the accompanying opinion. Pages 51–63 of the initial decision are not adopted.

It is further ordered, That the complaint be dismissed.

Commissioner Dixon dissents.

IN THE MATTER OF

NATIONAL INDUSTRIES, INC., ET AL.

ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 8859. Complaint, July 15, 1971 — Dismissal Order, June 18, 1979

This order dismisses a complaint charging a Louisville, Ky. firm and its wholly-owned subsidiary with illegally imposing geographic restrictions on licensed bottlers of their soft drink products, on the grounds that the companies are no longer engaged in the soft drink business or the practices which were the focus of the complaint.

Appearances

For the Commission: *Ronald L. Bloch.*

For the respondents: *Charles Kadish, Breed, Abbott & Morgan,* New York City and *Paul N. Kiel,* Fuqua Industries, Inc., Atlanta, Ga.

COMPLAINT

The Federal Trade Commission, having reason to believe that National Industries Inc. and its wholly-owned subsidiary, Cott Corporation, each hereby made and sometimes hereinafter referred to as respondent(s), have violated the provisions of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45), and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating its charges in that respect as follows:

PARAGRAPH 1. For the purposes of this complaint, the following definitions shall apply:

(a) Bottler — any individual, partnership, corporation, association or other business or legal entity which purchases respondents' concentrate for use in the manufacturing and sale, primarily at wholesale, of pre-mix or post-mix syrups or soft drink products or who purchases pre-mix or post-mix syrups or soft drink products for resale, primarily at wholesale;

(b) Central warehousing — a method of distribution in which soft drink products are received at a storage facility and either resold or delivered to retail outlets or wholesalers;

(c) Concentrate — the basic soft drink ingredient sold to bottlers by respondents, which is combined with water and other ingredients for packaging in bottles or cans for sale and distribution as soft drink products, or is used to make post-mix and pre-mix syrups;

(d) Consignment — a form of distribution in which the consignor retains title, dominion, bears all risks of loss and delivers his products to the consignee who is indistinguishable from a salesman or agent;

(e) Place of business — the location of any facilities available to a bottler without regard to customers or geographic area for production or service in the conduct of business operations, to include but not limited to business headquarters, branch sales offices, warehouses and garages, but specifically excluding the plant at which a bottler combines concentrate with water, and possibly other ingredients, for the packaging of soft drink products;

(f) Post-mix syrup — soft drink concentrate which is used in fountain dispensing or vending equipment and is usually sold by bottlers in steel tanks. A typical post-mix system draws one ounce of syrup from a five-gallon tank and mixes it at the point of sale with six ounces of carbonated water to produce 600 six-ounce finished soft drink servings per tank;

(g) Pre-mix syrup — although essentially the same syrup as post-mix, a pre-mix system differs from a post-mix system in that it draws from a five-gallon tank a serving of soft drink products containing both syrup and carbonated water to produce 100 six-ounce finished soft drink servings;

(h) Soft drink products — nonalcoholic beverages and colas, carbonated and uncarbonated, flavored and non-flavored, sold in bottles and cans, or through pre-mix and post-mix systems or the like.

PAR. 2. Respondent National Industries Inc., is a corporation organized, existing and conducting its business under and pursuant to the laws of the Commonwealth of Kentucky. It maintains its office and principal place of business at 510 West Broadway, Louisville, Kentucky. In 1968, respondent National Industries Inc. had net sales of $353,310,000 and assets of $283,771,000.

Respondent Cott Corporation, a wholly-owned subsidiary of National Industries Inc., is a corporation organized, existing and conducting its business pursuant to the laws of the State of New Hampshire. It maintains its office and principal place of business at 197 Chatham St., New Haven, Connecticut; owns and operates a concentrate manufacturing plant at Hamden, Connecticut; and operates soft drink bottling plants at South Portland, Maine, Millis and Somerville, Massachusetts, Pawtucket, Rhode Island, New

Haven, Connecticut, Manchester, New Hampshire, Bronx, New York, Elizabeth, New Jersey, Braddock, Pennsylvania and Miami, Florida. In 1968, respondent made sales to over 100 domestic bottlers located in 29 States throughout the United States.

PAR. 3. Respondent National Industries Inc., through various subsidiaries, is engaged in diverse businesses including sale of soft drink products and concentrate, dairy products, laboratory furniture, energy products and steel service centers. Its Consumer Products Division, with which respondent Cott Corporation is affiliated, accounted for $215,383,000, or 57% of total revenue in 1969.

Respondent Cott Corporation is engaged principally in the manufacture and sale of soft drink products and concentrate under its name, Cott, and under the names of its wholly-owned subsidiaries, Clicquot Club Company and Mission of California, Inc. In addition to its business as a bottler, respondent Cott sells soft drink products and concentrate to over 100 bottlers, who purchase under license to produce and sell soft drink products under such trade names of respondent as "Cott," "Clicquot Club," "Mission," "Quiky," "Energade" and "Big Giant Cola." Bottlers combine the concentrate with water and other ingredients and then package the mixture in bottles and cans for resale as soft drink products to retailers.

PAR. 4. Respondents are engaged in "commerce" within the meaning of the Federal Trade Commission Act (15 U.S.C. 44) in that National Industries Inc., through its wholly-owned subsidiary Cott Corporation, causes a continuous flow of interstate commerce in soft drink products and concentrate to exist between Cott Corporation headquarters and production facilities in New Haven and Hamden, Connecticut, and the numerous bottlers and retailers located throughout the United States which purchase their products.

PAR. 5. In the course and conduct of their businesses, respondents, except to the extent limited by the acts, practices and methods of competition hereinafter alleged, have been and are now in competition with other corporations, firms, partnerships and persons engaged in the manufacture, processing, distribution and sale of soft drink products in commerce.

PAR. 6. Respondents have hindered, frustrated, lessened and eliminated competition in the distribution and sale of pre-mix concentrates and soft drink products sold under their trade names by restricting their bottlers from selling outside of a designated geographical area. This restriction is set forth in the franchise agreement between respondents and their bottlers.

A typical agreement between respondent Cott Corporation and its bottlers provides that the bottler agrees:

To aggressively merchandise, promote, advertise and maintain the sales and distribution of Products in the territory covered by this Franchise Agreement, and to restrict distribution of Products produced by BOTTLER within the territory covered by this Franchise Agreement, and not permit the shipment, either directly or indirectly, of Products produced by BOTTLER into territories outside of the territory covered by this Franchise Agreement. In the event any other authorized franchisee of Products should, without authority of COMPANY, ship or permit to be shipped, any Product or Product Base into the exclusive territory covered by this Franchise Agreement, (except where said other authorized franchisee sold and delivered said Product Base to a customer within their territorial limits) COMPANY agrees to take appropriate action to prevent the continuation of such unauthorized acts, but shall not be liable in damages to the BOTTLER by reason of such unauthorized shipments, COMPANY'S obligations in this respect being limited to the exercising of the highest good faith to prevent such act or acts.

PAR. 7. The aforesaid agreements used by respondent Cott have had, and may continue to have, the following effects:

(a) Competition between and among respondent Cott's bottlers in the distribution and sale of "Cott," "Clicquot Club," "Mission," "Quiky," "Energade" and "Big Giant Cola" brands of soft drink products has been eliminated;

(b) Competition between and among Cott's bottling operations and its bottlers in the distribution and sale of Cott soft drink products at the wholesale level has been eliminated;

(c) Innumerable retailers and other customers have been deprived of the right to purchase "Cott," "Clicquot Club," "Mission," "Quiky," "Energade" and "Big Giant Cola" brands of soft drink products from the bottler of their choice at a competitive price; and

(d) Consumers of "Cott," "Clicquot Club," "Mission," "Quiky," "Energade" and "Big Giant Cola" brands of soft drink products have been deprived of the opportunity of obtaining such products in an unrestricted market and at competitive prices.

PAR. 8. Respondents' contracts, agreements, acts, practices and methods of competition aforesaid have had and may continue to have, the effect of lessening competition in the advertising, merchandising, distribution, offering for sale and sale of pre-mix concentrates and soft drink products; deprive, and may continue to deprive, the public of the benefits of competition in the purchase of soft drink products; and constitute unfair methods of competition and unfair acts or practices, in commerce, in violation of Section 5 of the Federal Trade Commission Act.

(Official National Industries Inc. Stationery)

(Date)

Dear

The Federal Trade Commission has entered an order against National Industries Inc. and Cott Corporation which among other things prohibits them from limiting, allocating or restricting the territory, persons or class of persons to whom our bottlers may sell. In addition, the order prohibits National Industries Inc. and Cott Corporation from restricting the location of the bottler's place of business or requiring an allocation of fees between one bottler and other bottlers for sales to any particular customer or in any geographical area.

National Industries Inc. and Cott Corporation are also prohibited from refusing to sell or threatening to refuse to sell to any bottler anything used in the manufacture and sale of soft drink products. Furthermore, National Industries Inc. and Cott Corporation are prohibited from requiring or requesting any bottler to, in any manner, inform them of the territories in which, or the person or class of persons (including but not limited to central warehousing customers) to whom the bottler sells, or attempts to sell, soft drink products, or pre-mix or post-mix syrups. A copy of the order is attached.

The Federal Trade Commission has expressed its intention to determine the effect upon the marketing of soft drink products caused by the attached order by ascertaining at some future date the extent to which sales of soft drink products by bottlers extend to customers outside of previously established, but now prohibited, territorial restrictions.

Very truly yours,

Initial Decision Dismissing Complaint by Joseph P. Dufresne, Administrative Law Judge

April 23, 1979

Preliminary Statement

The complaint in this matter is one of eight which issued against bottlers of soft drinks on July 15, 1971, challenging the geographic restrictions on franchisees established by the bottler/franchisors. Of these complaints, those against *The Coca-Cola Company, et al.* (Dkt. 8855) and *PepsiCo, Inc.* (Dkt. 8856) have been litigated and decisions [2] by the administrative law judge and the Commission have issued. The decisions against The Coca-Cola Company, et al. and PepsiCo presently are on appeal to the U.S. Circuit Court of Appeals for the District of Columbia.

The proceedings in connection with the complaints against the six other bottlers charged (*i.e. Crush International Limited, et al.* (Dkt. 8853) *Dr Pepper Company* (Dkt. 8854), *The Seven-Up Company* (Dkt. 8857), *Royal Crown Cola Company* (Dkt. 8858), *National Industries/Cott* (Dkt. 8859) and *Norton Simon, Inc./Canada Dry* (Dkt.

8877)) have been held in abeyance pending the outcome of the appeals in the *Coke* and *Pepsi* cases. No adjudicative hearings have been held in these six matters. (*See* "ORDER RE INTENTIONS OF RESPONDENTS IN UNLITIGATED 'BOTTLER' CASES" dated December 15, 1975, and "ORDER RE SUSPENDING HEARINGS IN SIX REMAINING 'BOTTLER' CASES PENDING APPELLATE COURT REVIEW OF COMMISSION'S COCA-COLA AND PEPSICO DECISIONS" dated September 19, 1978.)

DISCUSSION

In a letter/motion requesting dismissal of this complaint as to National, counsel for respondents National Industries, Inc. and Cott Corporation advised that neither firm is engaged any longer in the soft drink business or in the practices which are the subject of this matter. Commission counsel does not oppose the letter/motion. Counsel for respondents advised that the acquirer of Cott is dissolving it. (*See* letter from Charles Kadish, Esq. to me dated February 14, 1979, and "ORDER PLACING LETTER APPLICATION FOR DISMISSAL ON THE PUBLIC RECORD" dated February 27, 1979.) Commision counsel has advised that there is no information as to whether a "New Cott Corporation," which is reported to be conducting the soft drink business of respondent Cott, is engaging in the challenged practices. (*See* "COMPLAINT COUNSEL'S RESPONSE TO RESPONDENT'S MOTION TO DISMISS THE COMPLAINT AS TO NATIONAL INDUSTRIES, INC.," dated April 18, 1979.)

In these circumstances, it would be to the interest of the public, the Commission and respondents if the complaint were dismissed. Accordingly, and pursuant to authority contained in Commission Rules 3.22(a)(e), 3.24(a)(2), 3.42(c) and 3.51, [3]

ORDER

It is ordered, That the complaint in Dkt. 8859 against respondents National Industries, Inc., and Cott Corporation be, and it is hereby, dismissed.

FINAL ORDER

The administrative law judge filed his initial decision in this matter on April 23, 1979, dismissing the complaint against respondents National Industries, Inc. and Cott Corporation on grounds that neither respondent is now engaged in the soft drink business nor in the practices which were the focus of the complaint. No appeal from the initial decision was filed.

The Commission having now determined that the matter should not be placed on its own docket for review, and that the initial decision should become effective as provided in Section 3.51(a) of the Commission's Rules of Practice,

It is ordered, That the initial decision and order contained therein shall become effective on June 18, 1979.

IN THE MATTER OF

COOPER INDUSTRIES, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SECTION 5 OF THE FEDERAL TRADE COMMISSION ACT AND SECTION 7 OF THE CLAYTON ACT

Docket C-2970. Complaint, June 18, 1979 — Decision, June 18, 1979

This consent order, among other things, requires a Houston, Texas manufacturer of hand tools, compressors and other products used by the oil and gas industries to timely divest, subject to FTC approval, its Rotor Tool Division and the gas compressor business acquired through its merger with the Gardner-Denver Company. Additionally, the firm is barred for ten years from acquisitions in the two product areas without prior Commission approval.

Appearances

For the Commission: *Tom D. Smith, Harry L. Hobgood, Marilyn L. Richmond, Robert C. Jones* and *Dennis F. Johnson.*

For the respondent: *Richard P. Keeton, Vinson & Elkins,* Houston, Texas.

COMPLAINT

The Federal Trade Commission, having reason to believe that Cooper Industries, Inc. ("Cooper"), a corporation subject to the jurisdiction of the Commission, has entered into a merger agreement which, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45; that said agreement constitutes a violation of Section 5 of the Federal Trade Commission Act, as amended; and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, stating its charges as follows:

I. Definitions

1. For purposes of this complaint, the following definitions apply:

(a) "Compressors" means machines which elevate gaseous materials (including air, natural gas, and process gases such as oxygen and nitrogen) to higher pressures.

(b) "Reciprocating gas compressors" means machines which are used to elevate natural gas to higher pressures by confining successive volumes of the gas within a closed space, and in which the compressing element is a piston which has a reciprocating motion within a cylinder.

(c) "Integral reciprocating gas compressors" means reciprocating gas compressors in which the compressor and the driving engine are enclosed in a common casting, and in which both the driving pistons and the compressing pistons are connected to a common crankshaft.

(d) "Separable reciprocating gas compressors" means reciprocating gas compressors manufactured independently of the engines used to drive them.

(e) "Hand-held Industrial Pneumatic tools" means all tools that are powered by air motors, and which are utilized, or designed to be utilized, in or for manufacturing operations and are operated, or designed to be operated, while being held or supported by an individual's hands, and includes air motors capable of powering such tools and parts for all such tools or motors.

II. The Acquisition

2. On January 22, 1979, Cooper and Gardner-Denver Company ("G-D") entered into agreements whereby Cooper plans to acquire G-D in a transaction valued at approximately $630.3 million. Under the terms of the agreements, Cooper commenced a cash tender offer on February 14, 1979 for 8.6 million shares of G-D common stock, constituting approximately 45 percent of G-D's outstanding common shares. Approximately 12.6 million shares were tendered before the expiration of the offer. Following completion of the tender offer, Cooper intends to acquire the remaining 55 percent of G-D's common stock through an exchange of G-D common shares for fractional shares of Cooper common stock and a new issue of Cooper convertible preferred stock, with the merger scheduled for completion on or about April 30, 1979.

III. Cooper Industries, Inc.

3. Cooper is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Ohio, with its principal place of business located at Two Houston Center, Houston, Texas.

4. Cooper is a major manufacturer of compressors and other supplies for the oil and gas industries, a major manufacturer of hand tools, and also provides overhaul and repair services for aircraft jet engines.

5. In 1978, Cooper had total revenues of $782.0 million, net income of $68.2 million, assets of $360.4 million, and was ranked by

Fortune magazine as the nation's 307th largest industrial company based on 1977 sales of $678.8 million.

6. Cooper's Cooper-Bessemer division manufactures large gas compressors in sizes ranging from 900 horsepower to 30,000 horsepower. Cooper's Ajax division manufactures integral reciprocating gas compressors in sizes ranging from 30 horsepower to 600 horsepower. Cooper's Superior division manufactures separable reciprocating gas compressors in sizes ranging from 300 horsepower to 2,750 horsepower. In 1978, Cooper's Ajax and Superior divisions had total sales of reciprocating gas compressors of approximately $40.0 million.

7. Cooper's Rotor Tool Division manufactures and sells a broad line of hand-held industrial pneumatic tools. In 1978, Cooper's sales of hand-held industrial pneumatic tools were approximately $12.0 million.

IV. Gardner-Denver Company

8. G–D is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware with its principal place of business located at 8585 Stemmons Freeway, Dallas, Texas.

9. G–D manufactures a wide range of drilling equipment used by the construction, petroleum and mining industries, and is also a major producer of compressors, hand-held industrial pneumatic tools and other industrial products.

10. G–D had 1978 revenues of $652.0 million, net income of $51.4 million, assets of $387.1 million, and was ranked by Fortune magazine as the nation's 389th largest industrial company based on 1977 sales of $502.4 million.

11. G–D is a major manufacturer of compressors. G–D manufactures and sells reciprocating gas compressors in sizes ranging from 20 horsepower to 650 horsepower. In 1978, G–D had total sales of reciprocating gas compressors of approximately $1.9 million.

12. Through its Pneutronics Division, G–D manufactures and sells a broad line of hand-held industrial pneumatic tools. In 1978, total sales by G–D of hand-held industrial pneumatic tools were approximately $19.5 million.

V. Jurisdiction

13. At all times relevant to this complaint, Cooper and G–D have been engaged in the manufacture and sale of various products, including those products relevant to this complaint, in interstate

commerce and have been engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. 12. At all times relevant to this complaint, the businesses of both Cooper and G-D have been in or affecting commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

VI. Trade and Commerce

14. The relevant markets are:

a. The manufacture in the United States of reciprocating gas compressors in sizes ranging from 30 horsepower to 1,000 horsepower, and the sale of such compressors, as well as any submarket thereof.

b. The manufacture in the United States of hand-held industrial pneumatic tools, and the sale of such tools, as well as any submarket thereof.

VII. Actual Competition

15. Cooper and G-D are now, and have been since at least 1973, actual competitors of each other in both of the relevant markets enumerated in Paragraph Fourteen of this complaint.

A. Reciprocating Gas Compressors

16. In 1978, Cooper was the largest domestic manufacturer of reciprocating gas compressors in sizes ranging from 30 horsepower to 1,000 horsepower, in terms of units shipped, with a market share of approximately 30%. In 1978, G-D was the seventh largest manufacturer of reciprocating gas compressors in sizes ranging from 30 horsepower to 1,000 horsepower, in terms of units shipped, with a market share of approximately 3%.

17. In 1978, the market share of the top four domestic manufacturers was over 60%, in terms of units shipped, for reciprocating gas compressors from 30 horsepower to 1,000 horsepower.

18. G-D and Cooper compete in the manufacture and sale of reciprocating gas compressors ranging in size from 30 horsepower to 1,000 horsepower.

B. Hand-held Industrial Pneumatic Tools

19. In 1977, G-D was the third largest manufacturer of hand-held industrial pneumatic tools with a market share of 10.0%, in terms of dollar sales. In 1977, Cooper was the fifth largest manufacturer of hand-held industrial pneumatic tools with a market share of 5.5%, in terms of dollar sales.

20. In 1978, the market share of the top four domestic manufac-

turers was over 60%, in terms of dollar sales, for hand-held industrial pneumatic tools.

21. G-D and Cooper compete in the manufacture and sale of hand-held industrial pneumatic tools.

IX. Effects of the Acquisition

22. The effects of the proposed acquisition may be to substantially lessen competition or tend to create a monopoly in the relevant markets enumerated in Paragraph Fourteen of this complaint in the following ways, among others:

(a) actual competition between Cooper and G-D in the manufacture and sale of reciprocating gas compressors will be eliminated;

(b) concentration in the manufacture and sale of reciprocating gas compressors will be increased and the possibilities for eventual deconcentration may be diminished;

(c) actual competition between Cooper and G-D in the manufacture and sale of hand-held industrial pneumatic tools will be eliminated; and

(d) concentration in the manufacture and sale of hand-held industrial pneumatic tools will be increased and the possibilities for eventual deconcentration may be diminished.

X. Violations Charged

23. The proposed acquisition set forth in Paragraph Two, if consummated, would violate Section 7 of the Clayton Act, as amended, (15 U.S.C. 18).

24. The proposed acquisition set forth in Paragraph Two, if consummated, would violate Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

25. The merger agreements described in Paragraph Two violate Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

Decision and Order

The Federal Trade Commission, having initiated an investigation of the proposed acquisition of Gardner-Denver Company by Cooper Industries, Inc. (hereinafter referred to as "Cooper"), and Cooper having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Cooper with violation of Section 7 of the

Clayton Act (15 U.S.C. 18) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45); and

Cooper, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by Cooper of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by Cooper that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Cooper has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Cooper is a corporation organized, existing and doing business under and by virtue of the laws of the State of Ohio, with its office and principal place of business located at Two Houston Center, Houston, Texas.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Cooper, and the proceeding is in the public interest.

Order

I

It is ordered, That the following definitions shall apply herein:

(1) "Reciprocating gas compressors" means all machines which are used to elevate natural gas to higher pressures by confining successive volumes of the gas within a closed space, and in which the compressing element is a piston which has a reciprocating motion within a cylinder.

(2) "Hand-held industrial pneumatic tools" means all tools that are powered by air motors, and which are utilized, or designed to be utilized, in or for manufacturing operations and are operated, or designed to be operated, while being held or supported by an individual's hands, and includes air motors capable of powering such tools and parts for all such tools or motors.

(3) "Gas compressor business" means the Gardner-Denver Compa-

ny's ML Horizontal Series, RL and RLT Horizontal Series, LA and LB Vertical Series, AOL Vertical "V" Type Air Cooled Series product line of reciprocating gas compressors, related parts, developmental units (including the 13F and MLQ) and the jigs, patterns, dies, designs, drawings, technical data and literature, appropriate royalty-free license for all patents and patent applications, bills of materials and specialized goods that are unique to, or necessary for, the manufacture of such reciprocating gas compressors and which are currently in existence or which are produced prior to divestiture.

(4) "Rotor Tool Division" means the Rotor Tool Division of Cooper, and includes all assets, properties, titles to property, interests, rights and privileges of whatever nature, tangible and intangible, including, but not limited to, all real property, buildings, machinery, equipment, tools, raw materials, inventory, customer lists, trade names, patents, patent applications, trademarks and all other property of whatever description presently owned or operated by Cooper for the manufacture of the products produced by the Rotor Tool Division, together with all additions, replacements, and improvements hereafter made by Cooper to the Rotor Tool Division.

II

It is further ordered, That Cooper, its officers, directors, agents, representatives and employees shall:

(1) Within twelve (12) months from the date this order becomes final, divest absolutely, to an acquiror which meets with the prior approval of the Federal Trade Commission, the gas compressor business acquired by Cooper as a result of its merger with Gardner-Denver Company; and

(2) Within eighteen (18) months from the date this order becomes final, divest absolutely, with the prior approval of the Federal Trade Commission, the Rotor Tool Division as a going concern in the manufacture and sale of hand-held industrial pneumatic tools.

III

It is further ordered, That in connection with the divestiture of the gas compressor business required by Paragraph II of this order, Cooper shall offer to any prospective acquiror the right to enter into a contract to buy from Cooper, if Gardner-Denver Company manufactured them during any part of the calendar year 1978, replacement parts for, and parts normally used in or for the gas compressor business (excluding parts for developmental equipment), which contract will, at the acquiror's option, include one or both of the following provisions:

(1) The contract will continue for a minimum of two (2) years or for a shorter period of time at the sole discretion of the acquiror;

(2) Prices for such replacement parts and parts will be not more than inventory cost (before any adjustment for LIFO valuation) as of the date of divestiture plus 29% of such inventory cost during the first twelve (12) month period and plus 50% of such inventory cost during the second twelve (12) month period. Further, the acquiror shall have the right to have Cooper's books and accounts inspected by an independent accounting firm, which firm shall be subject to approval by Cooper, and which approval shall not be unreasonably withheld, for the purpose of confirming such inventory cost.

IV

It is further ordered, That in connection with the divestiture of the gas compressor business required by Paragraph II of this order, Cooper shall:

(1) Make available, at their place of employment, all former Gardner-Denver personnel in the employ of Cooper who are familiar and associated with the gas compressor business for advice and assistance and such detailed explanation of the gas compressor business as the acquiror may request for a period of one (1) year following the date of divestiture;

(2) License royalty-free, for a period of two (2) years following the date of divestiture, the name "Gardner-Denver" to the acquiror for use in connection with the gas compressor business;

(3) Not use, in connection with the manufacture or sale of reciprocating gas compressors, for a period of two (2) years following the date of divestiture, the name "Gardner-Denver;"

(4) Refrain, for a period of five (5) years from the date of divestiture, from manufacturing or selling the reciprocating gas compressors comprising the gas compressor business or replacement parts for use in the gas compressor business, except in accordance with Paragraph III of this order, *provided, however,* that Cooper shall have the right to sell replacement parts to owners of such reciprocating gas compressors if, after Cooper has notified the acquiror in writing, the acquiror fails to provide parts for such reciprocating gas compressors within ninety (90) days.

V

It is further ordered, in connection with the divestiture of the

Rotor Tool Division required by Paragraph II of this order, that Cooper shall:

(1) Beginning 20 days after the date this order becomes final, until divestiture, maintain and operate the Rotor Tool Division as a separate division with separate books and accounts, separate management, separate assets, and separate personnel, and not transmit, or permit the transmittal of, the Rotor Tool Division's technical data, marketing plans or pricing information to Cooper, except that Cooper may continue to receive the Rotor Tool Division's profit forecasts and continue to monitor the Rotor Tool Division's performance against such forecasts, and may continue to provide the following corporate services: banking, industrial relations, legal, insurance, safety, tax, and pension management;

(2) Not sell, lease, otherwise dispose of, or encumber, without the consent of the Federal Trade Commission, any substantial property or other assets of the Rotor Tool Division;

(3) Prior to divestiture, not hire or employ, except as an employee of the Rotor Tool Division, any individual employed by the Rotor Tool Division during any part of the period from March 15, 1979, to the date of divestiture without the prior approval of the Federal Trade Commission, except for the following named individuals: Frank X. Linsenmeyer, Jr., and E. Ralph Smith III; *provided* that such named individuals shall not be associated with the Rotor Tool Division in any way for more than one (1) year from the date this order becomes final, unless such individuals are hired or employed by the acquiror; and *further provided* that Cooper shall not interfere in any way with the acquiror's soliciting employment agreements from, or negotiating employment agreements with, such named individuals;

(4) For a period of three (3) years following divestiture, not hire or employ, without the prior approval of the Federal Trade Commission, any individual employed by the Rotor Tool Division during any part of the period from March 15, 1979 to the date of divestiture;

(5) Pending divestiture, maintain the Rotor Tool Division as an independent entity and take no action to impair such entity's economic or financial position; and

(6) Pending divestiture, not allow the deterioration of the Rotor Tool Division in a manner that impairs its viability.

VI

It is further ordered, That Cooper shall cease and desist, for a period of ten (10) years from the date this order becomes final, from acquiring, directly or indirectly, through subsidiaries or otherwise, without the prior approval of the Federal Trade Commission, the whole or any part of the stock or share capital of any corporate or noncorporate concern engaged in the United States in, or any assets utilized in, the manufacture, distribution, importation or sale of (a) reciprocating gas compressors in sizes ranging from 30 to 1,000 horsepower, or powered by engines in sizes ranging from 30 to 1,000 horsepower, or (b) hand-held industrial pneumatic tools.

VII

It is further ordered, That Cooper shall, within sixty (60) days from the date this order becomes final, and every sixty (60) days thereafter until Cooper has accomplished the divestitures required by Paragraph II of this order, submit in writing to the Federal Trade Commission a verified report setting forth in detail the manner and form in which Cooper intends to comply or has complied with Paragraphs II, III, IV and V of this order. All such reports shall include a summary of contacts or negotiations with anyone for the specified assets, the identity of all such persons, and copies of all written communications to and from such persons.

VIII

It is further ordered, That annually on the anniversary of the date this order becomes final, for a period of ten (10) years, Cooper shall submit in writing to the Federal Trade Commission a verified report setting forth in detail the manner and form in which Cooper intends to comply or has complied with Paragraph VI of this order.

IX

It is further ordered, That Cooper notify the Federal Trade Commission at least thirty (30) days prior to any proposed change in Cooper which may affect compliance obligations arising out of the order, such as dissolution, assignment or sale resulting in the emergence of a successor corporation or the creation or dissolution of subsidiaries.

In the Matter of

ARNAUDVILLE INDUSTRIES, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND MAGNUSON-MOSS WARRANTY ACTS

Docket C-2972. Complaint, June 21, 1979 — Decision, June 21, 1979

This consent order, among other things, requires an Arnaudville, La. manufacturer and seller of mobile homes to cease improperly designating its warranties; and failing to include in its warranties all the information required by the Disclosure Rule, 16 CFR 701 (1977). The order further requires that purchasers of firm's products manufactured after July 4, 1975, whose warranties are still in effect, be informed, as prescribed, of their legal rights and the firm's obligations under warranties.

Appearances

For the Commission: *Michael E.K. Mpras, Bernard Fensterwald III* and *Rachel Miller.*

For the respondent: *Robert G. Szabo,* Arnaudville, La.

Complaint

Pursuant to the provisions of the Federal Trade Commission Act, as amended, and of the Magnuson-Moss Warranty-Federal Trade Commission Improvement Act ("Warranty Act") and the implementing rules promulgated under the Warranty Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Arnaudville Industries, Inc., a corporation, sometimes referred to in the complaint as respondent, has violated the provisions of said Acts and implementing rules, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Arnaudville Industries, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Louisiana with its principal office and place of business located at Highway 31, P.O Box 79, Arnaudville, Louisiana.

PAR. 2. Respondent has been, and is now, engaged in the manufacture, distribution and sale of mobile homes to the public.

PAR. 3. In the course and conduct of its business, respondent is a supplier of consumer products distributed in commerce, as "supplier," "consumer product," and "commerce" are defined by Sections 101(4), 101(1) and 101(13) and (14) of the Warranty Act respectively. In connection with the distribution in commerce of its consumer products, manufactured subsequent to July 4, 1975, respondent offers a written warranty, as "written warranty" is defined by Section 101(6) of the Warranty Act, and is therefore a warrantor, as "warrantor" is defined by Section 101(5) of the Warranty Act.

COUNT I

Alleging violations of the Warranty Act and the Federal Trade Commission Act, as amended, the allegations of Paragraphs One through Three are incorporated by reference in Count I as if fully set forth verbatim.

PAR. 4. In connection with respondent's offering and granting of written warranties on its mobile homes, respondent failed to clearly and conspicuously designate each such warranty as either a "full (statement of duration) warranty" or a "limited warranty."

PAR. 5. Respondent's failure to designate its warranties as described in Paragraph Four of this complaint is a violation of Section 103 of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

PAR. 6. In connection with its written warranty, respondent has designated such warranty as a "FULL ONE YEAR LIMITED WARRANTY." The use by respondent of such designation has had and continues to have the capacity and tendency to mislead consumers as to the nature or scope of the warranty.

PAR. 7. Respondent's designation of its written warranties as described in Paragraph Six of this complaint constitutes a deceptive warranty in violation of Section 110(c)(2) of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT II

Alleging violations of the Warranty Act and the implementing rule promulgated under the Warranty Act, and the Federal Trade Commission Act, as amended, the allegations of Paragraphs One through Three are incorporated by reference in Count II as if fully set forth verbatim.

PAR. 8. The Federal Trade Commission, pursuant to Title I, Section

109 of the Warranty Act, (15 U.S.C. 2309), duly promulgated the Rule concerning the Disclosure of Written Consumer Product Warranty Terms and Conditions on December 31, 1975 (16 CFR 701 (1977)) (effective January 1, 1977) ("Disclosure Rule"). A copy of the Disclosure Rule is marked and attached as Appendix A* and is incorporated in Count II by reference as if fully set forth verbatim.

PAR. 9. Subsequent to January 1, 1977, in connection with its offering and granting of written warranties on mobile homes, which were manufactured subsequent to January 1, 1977, respondent failed to clearly and conspicuously disclose, in a single document, in simple and readily understood language, the following information:

(1) A statement in the following language as required by Section 701.3(a)(9) of the Disclosure Rule:

This warranty gives you specific legal rights, and you may also have other rights which vary from state to state.

(2) A statement in the following language as required by Section 701.3(a)(8) of the Disclosure Rule:

Some states do not allow the exclusion or limitation of incidental or consequential damages, so the above limitation or exclusion may not apply to you.

PAR. 10. Respondent's failure to comply with the Disclosure Rule as described in Paragraph Nine of this complaint is a violation of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act, the Magnuson-Moss Warranty — Federal Trade Commission Improvement Act ("Warranty Act"), and the Rule Concerning the Disclosure of Written Consumer Product Warranty Terms and Conditions ("Disclosure Rule"); and

The respondent, its attorney, and counsel for the Commission

* Not reported herein for reasons of economy.

having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Arnaudville Industries, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Louisiana, with its office and principal place of business located at Highway 31, P.O. Box 79, in the City of Arnaudville, State of Louisiana.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

I. Definitions

For the purposes of this order the definitions of the terms "written warranty" and "consumer product" as defined in Section 101 of the Warranty Act shall apply.

II.

It is ordered, That respondent Arnaudville Industries, Inc., a corporation, its successors and assigns, and its officers, representatives, agents and employees, directly or indirectly, through any corporation, subsidiary, division or any other device in connection with the advertising, offering for sale and sale of mobile homes and all other consumer products, do forthwith cease and desist from:

1. Offering or granting a written warranty on consumer products actually costing the consumer in excess of $10.00 which is not clearly and conspicuously designated as either a "full (statement of duration) warranty" or a "limited warranty."

having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Arnaudville Industries, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Louisiana, with its office and principal place of business located at Highway 31, P.O. Box 79, in the City of Arnaudville, State of Louisiana.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

I. Definitions

For the purposes of this order the definitions of the terms "written warranty" and "consumer product" as defined in Section 101 of the Warranty Act shall apply.

II.

It is ordered, That respondent Arnaudville Industries, Inc., a corporation, its successors and assigns, and its officers, representatives, agents and employees, directly or indirectly, through any corporation, subsidiary, division or any other device in connection with the advertising, offering for sale and sale of mobile homes and all other consumer products, do forthwith cease and desist from:

1. Offering or granting a written warranty on consumer products actually costing the consumer in excess of $10.00 which is not clearly and conspicuously designated as either a "full (statement of duration) warranty" or a "limited warranty."

2. Offering or granting a written warranty on consumer products actually costing the consumer in excess of $15.00, which fails to clearly and conspicuously disclose, in a single document, in simple and readily understood language, the following information:

This warranty gives your specific legal rights, and you may also have other rights which vary from state to state.

3. Offering or granting a written warranty on consumer products actually costing the consumer in excess of $15.00, and which excludes or limits relief such as incidental or consequential damages, which fails to clearly and conspicuously disclose, in a single document, in simple and readily understood language, the following information:

Some States do not allow the exclusion or limitation of incidental or consequential damages, so the above limitation or exclusion may not apply to you.

4. Offering or granting a written warranty on consumer products actually costing the consumer in excess of $15.00, which fails to comply with the Warranty Act, the Rule concerning the Disclosure of Written Consumer Product Warranty Terms and Conditions (16 CFR 701 (1977)) (effective January 1, 1977) ("Disclosure Rule"), the Rule concerning the Pre-Sale Availability of Written Warranty Terms (16 CFR 702 (1977)) (effective January 1, 1977) ("Pre-Sale Rule"), and the Rule concerning the Informal Dispute Settlement Procedures (16 CFR 703) (1977) (effective January 1, 1977).

III.

It is further ordered, That respondent:

A. Shall, in performing pursuant to its written warranties, meet the minimum requirements of Section 104 of the Magnuson-Moss Warranty — Federal Trade Commission Improvement Act ("Warranty Act") for all consumer products sold by respondent which are still under warranty as of the effective date of the order, and which were manufactured after July 4, 1975. This provision is limited to warranties issued by respondent which did not comply with the Warranty Act and the Disclosure Rule as stated in the complaint.

B. Notify all consumers affected by Paragraph A., above, by mailing to each such consumer the notice set forth in Appendix B of this order within 30 days from the effective date of the order. Respondent shall obtain the names and addresses of such consumers from its files and/or from the files of all retail outlets which sell respondent's products.

C. Shall not raise any defenses arising from the use of the terms

"Limited Warranty" in any case, suit or other proceeding brought against respondent by consumers affected by Paragraph A, above.

D. Notify, within 30 days from the effective date of the order, all its dealers who sell respondent's mobile homes, and all its agents and employees who are authorized to handle warranty claims, of all changes in its written warranties, including, but not limited to, consumer rights and remedies available to them under the warranty and this order.

E. Deliver a copy of this order to cease and desist to all present employees, salesmen, agents, independent contractors and other representatives engaged in the preparation and distribution of written warranties, and in the sale of warranted consumer products on behalf of respondent and secure a signed statement acknowledging receipt of the order from each such person.

F. Maintain complete records for a period of three (3) years from the effective date of the order to be furnished upon request to the staff of the Federal Trade Commission, including but not limited to, copies of complaints, requests for service, service records, letters mailed to consumers pursuant to Paragraph B of the order, written warranties, and any other written communications between respondent and its customers which relate to warranty service and performance.

G. Notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

H. Shall within sixty days (60) days after service upon it of this order, file with the Commission a report in writing, setting forth in detail the manner and form in which it has complied with this order.

APPENDIX B

[NAME AND ADDRESS OF CONSUMER] [DATE]

Dear [Name of Consumer]:

Following a review of our written warranty by the Federal Trade Commission, it was pointed out to us that we had made a few errors in our warranty. We have voluntarily agreed with the FTC to write you this letter as part of a way to correct those errors.

Now you have some added warranty protection for your mobile home.

The Federal Warranty Act requires warranties to be labeled as full warranties or as limited warranties. Because our warranty was titled "full one year limited warranty," we will treat it as a full warranty.

Here is what this means.

(1) If a manufacturing defect shows up in the first year since you got your home, we will fix it free. We will also pay for removal, reinstallation, on-site repairs and shipping if needed.

(2) We will fix the problem within a reasonable time after you tell us about it.

(3) If we try a reasonable number of times and still can't fix the problem, we will replace the defective part. If the problem is sufficiently serious and we can't fix it, we will either give you a new mobile home, or if you prefer, we will give you your money back. However, we will not be responsible for fixing any damage caused by your misuse or abuse of the home, or by such uncontrollable forces as lightning, floods, and the like.

Also, some parts of your mobile home, such as your kitchen appliances, carpets, draperies, furniture and other such items, are not covered by our written warranty. These items are covered by written warranties issued by other manufacturers as indicated in your Owner's Manual.

(4) If you sell your home during the first year, the new owner will get the same protection until the warranty ends. If you have already sold your home, please tell the new owner about this, or tell us and we will write to them.

Also, our warranty said we will not pay for any losses caused by a defective product. We want you to know that in some cases, and in some states, even these are covered.

If you have questions or problems, please feel free to contact your dealer. Or call us collect at (tele. no.). We will be glad to help.

Sincerely,

Arnaudville Industries, Inc.

FTC Dkt. C-2972, June 21, 1979.

IN THE MATTER OF

MADISON MOBILE-MODULAR HOMES, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND MAGNUSON-MOSS WARRANTY ACTS

Docket C-2973. Complaint, June 21, 1979 — Decision, June 21, 1979

This consent order, among other things, requires an Ontario, Calif. manufacturer and seller of mobile homes to cease failing to properly designate its written warranties; disclose in its warranties all the information required by the Disclosure Rule, 16 CFR 701 (1977); and note in its warranty registration cards that warranty coverage or performance is not conditioned on the return of the cards. The firm is further required to notify purchasers of respondent's mobile homes manufactured after July 4, 1975 of their implied warranty rights; and make available to these consumers all the relief provided under applicable state laws. Additionally, the order restrains the firm for four years from raising any defenses relating to the disclaimer of implied warranties in suits brought by affected purchasers.

Appearances

For the Commission: *Michael E.K. Mpras, Bernard Fensterwald III* and *Rachel Miller.*

For the respondent: *Dan Holden,* Anaheim, Calif.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, and of the Magnuson-Moss Warranty-Federal Trade Commission Improvement Act ("Warranty Act") and the implementing rules promulgated under the Warranty Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Madison Mobile-Modular Homes, Inc., a corporation ("respondent"), has violated the provisions of said Acts and implementing rules, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent is a corporation organized, existing and doing business under and by virtue of the laws of the State of California with its principal office and place of business located at 1555 S. Cucamonga Ave., Ontario, California.

PAR. 2. Respondent has been, and is now, engaged in the designing, manufacture, distribution and sale of mobile homes to the public.

Respondent distributes its mobile homes primarily in California, Arizona, and Nevada.

PAR. 3. In the course and conduct of its business, respondent is a supplier of consumer products distributed in commerce, as "supplier," "consumer product," and "commerce" and defined by Sections 101(4), 101(1) and 101(13) and (14), respectively, of the Warranty Act. In connection with the distribution in commerce of its consumer products, manufactured subsequent to July 4, 1975, respondent offers a written warranty, as "written warranty" is defined by Section 101(6) of the Warranty Act, and is therefore a warrantor, as "warrantor" is defined by Section 101(5) of the Warranty Act.

COUNT I

Alleging violations of the Warranty Act and the Federal Trade Commission Act, as amended, the allegations of Paragraphs One through Three are incorporated by reference in Count I as if fully set forth verbatim.

PAR. 4. In connection with respondent's offering and granting of written warranties on mobile homes which cost the consumer in excess of $10.00, respondent failed to clearly and conspicuously designate each such warranty as either a "full (statement of duration) warranty" or a "limited warranty."

PAR. 5. Respondent's failure to designate its warranties as described in Paragraph Four of this complaint is a violation of Section 103 of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT II

Alleging violations of the Warranty Act and the Federal Trade Commission Act, as amended, the allegations of Paragraphs One through Three are incorporated by reference in Count II as if fully set forth verbatim.

PAR. 6. In connection with respondent's offering and granting of written warranties on mobile homes, respondent has disclaimed all implied warranties available to consumers under state law with respect to the mobile homes sold by respondent, including the implied warranty of merchantability and the implied warranty of fitness for a particular purpose.

PAR. 7. Respondent's disclaimer of the implied warranties as described in Paragraph Six of this complaint is a violation of Section

108(a) of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT III

Alleging violations of the Warranty Act and the implementing rule promulgated under the Warranty Act, and the Federal Trade Commission Act, as amended, the allegations of Paragraphs One through Three are incorporated by reference in Count III as if fully set forth verbatim.

PAR. 8. The Federal Trade Commission, pursuant to Title I, Section 109 of the Warranty Act, (15 U.S.C. 2309), duly promulgated the Rule Concerning the Disclosure of Written Consumer Product Warranty Terms and Conditions on December 31, 1975 (16 CFR 701 (1977)) (effective January 1, 1977) ("Disclosure Rule"). A copy of the Disclosure Rule is marked and attached as Appendix A* and is incorporated in Count III by reference as if fully set forth verbatim.

PAR. 9. Subsequent to January 1, 1977, in connection with its offering and granting of written warranties on mobile homes costing the consumer in excess of $15.00 which were manufactured subsequent to January 1, 1977, respondent failed to clearly and conspicuously disclose, in each written warranty the following information:

(1) A statement in the following language as required by Section 701.3(a)(9) of the Disclosure Rule:

> This warranty gives you specific legal rights, and you may also have other rights which vary from state to state.

(2) A statement in the following language as required by Section 701.3(a)(8) of the Disclosure Rule:

> Some states do not allow the exclusion or limitation of incidental or consequential damages, so the above limitation or exclusion may not apply to you.

A step-by-step explanation of the procedure which the consumer should follow in order to obtain performance of any warranty obligation, including the persons or class of persons authorized to perform warranty obligations. This includes the name of the warrantor, together with the mailing address of the warrantor, and/or the name or title and the address of any employee or department of the warrantor responsible for the performance of warranty obligations, and/or a telephone number which consumers

* Not reported herein for reasons of economy.

may use without charge to obtain information on warranty performance, as required by Section 701.3(a)(5) of the Disclosure Rule.

PAR. 10. Respondent's failure to comply with the Disclosure Rule as described in Paragraph Nine of the complaint is a violation of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

PAR. 11. In connection with respondent's offering and granting of written warranties, respondent has made the following statements and representations in its written warranties and warranty coupons:

To validate this warranty, the warranty [sic], the warranty coupon attached hereto shall be fully executed and returned to the manufacturer within (5) days after the initial delivery of the mobile home to the original retail purchaser.

Return warranty coupon immediately to assure warranty . . .

Note: mail to Madison Mobile — Modular Homes, Inc., within three (3) days after delivery to address below where home was purchased.

PAR. 12. By and through the statements and representations described in Paragraph Eleven of the complaint, respondent has represented, directly or by implication, that the consumer's obligation to return the warranty coupon within five days (or three days) after delivery of the mobile home is a condition precedent to warranty coverage and performance.

PAR. 13. In truth and in fact, respondent, in many instances, does not require the return of the warranty coupon as a condition precedent to warranty coverage and performance. It is respondent's policy to service the mobile homes under warranty whenever the consumers demonstrate any reasonable evidence of date of purchase.

PAR. 14. The use by respondent of the statements and representations in its written warranties as described in Paragraph Eleven of this complaint has had and continues to have the capacity and tendency to mislead consumers into the mistaken and erroneous belief that warranty coverage and performance is only obtainable if the warranty coupon has been returned by the consumer within the stated time. Therefore, the statements and representations as set forth in Paragraph Eleven of the complaint were and are false, misleading and deceptive.

PAR. 15. Respondent's statements and representations as described in Paragraphs Eleven through Thirteen of the Complaint constitute a deceptive warranty in violation of Section 110(c)(2) of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, are unfair or deceptive acts or practices in violation of Section 5 of the Federal Trade Commission Act, as amended.

PAR. 16. In connection with its written warranties, respondent has failed to disclose in such warranties that the return of the warranty coupon is not a condition precedent to warranty coverage and performance, as required by Section 701.4 of the Disclosure Rule.

PAR. 17. Respondent's failure to comply with the Disclosure Rule as described in Paragraph Sixteen of the Complaint is a violation of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act, the Magnuson-Moss Warranty — Federal Trade Commission Improvement Act ("Warranty Act"), and the Rule Concerning the Disclosure of Written Consumer Product Warranty Terms and Conditions ("Disclosure Rule"); and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admisssion by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent, Madison Mobile-Modular Homes, Inc. is a corporation organized, existing and doing business under and by virtue of

the laws of the State of California, with its office and principal place of business located at 155 S. Cucamonga Ave., in the City of Ontario, State of California.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

I. Definitions

For the purposes of this order the definitions of the terms "written warranty" and "consumer product" as defined in Section 101 of the Warranty Act shall apply.

II.

It is ordered, That respondent Madison Modular-Mobile Homes, Inc., a corporation, its successors and assigns, and its officers, representatives, agents and employees, directly or indirectly, through any corporation, subsidiary, division or any other device in connection with the advertising, offering for sale and sale of mobile homes and all other consumer products, do forthwith cease and desist from:

1. Offering or granting a written warranty upon consumer products actually costing the consumer in excess of $10.00 which is not clearly and conspicuously designated as either a "full (statement of duration) warranty" or a "limited warranty."

2. Offering or granting a written warranty upon any consumer product which limits, modifies or disclaims, in any manner, the implied warranties available to the consumer, including, but not limited to, the implied warranty of merchantability and the implied warranty of fitness for a particular use; *provided, however,* that nothing contained in this paragraph shall prevent respondent from limiting the duration of such implied warranties to the duration of a limited written warranty pursuant to Section 108(b) of the Warranty Act (15 U.S.C. 2308(b)). Any such limitation shall be immediately followed by the statement specified in 16 CFR 701.3(a)(7).

3. Offering or granting a written warranty upon consumer products actually costing the consumer in excess of $15.00, which fails to clearly and conspicuously disclose in the warranty the following items of information:

(a) A statement in the following language:

This warranty gives you specific legal rights, and you may also have other rights which vary from state to state.

(b) A step-by-step explanation of the procedure which the consumer should follow in order to obtain performance of any warranty obligation, including the persons or class of persons authorized to perform warranty obligations. This includes the name of the warrantor, together with the mailing address of the warrantor, and/or the name or title and the address of any employee or department of the warrantor responsible for the performance of warranty obligations, and/or a telephone number which consumers may use without charge to obtain information on warranty performance.

4. Offering or granting a written warranty upon consumer products actually costing the consumer in excess of $15.00, and which excludes or limits relief such as incidental or consequential damages, which fails to clearly and conspicuously disclose in the warranty a statement in the following language:

Some states do not allow the exclusion or limitation of incidental or consequential damages, so the above limitation or exclusion may not apply to you.

5. Offering or granting a written warranty upon any consumer product actually costing the consumer in excess of $15.00 which employs the use of any card such as an owner's registration card, warranty registration card, warranty coupon, or the like, unless it is clearly and conspicuously disclosed in the warranty that the return of such card or coupon is not a condition precedent to warranty coverage and performance.

6. Offering or granting a written warranty on consumer products actually costing the consumer in excess of $15.00, which fails to comply with all of the requirements of the Warranty Act and amendments thereto, and all rules promulgated thereunder.

It is further ordered, That respondent:

A. Label or title its warranty coupon, owner's registration card, warranty registration card, or the like, according to the purpose or purposes for which it is intended, *e.g.,* "marketing research card."

B. Disclose, clearly and conspicuously, in simple and readily understood language, and in the largest type that appears on the warranty coupon (appropriately labeled pursuant to paragraph A., above,) the following information:

1. The purpose(s) for which such coupon or card is utilized.

2. That the consumer is not required to fill out or mail the coupon or card for, or as a condition precedent to, warranty coverage and performance.

C. For four years after the effective date of the order:

1. Shall not raise any defenses pertaining to the disclaimer of implied warranties in any case, suit or other proceeding brought against respondent by consumers who have purchased any of respondent's warranted products manufactured between July 4, 1975 and the effective date of the order.

2. Provide all consumers who have purchased any of respondent's warranted products manufactured between July 4, 1975 and the effective date of the order, which do not comply with all of the implied warranties, with all relief available to them by applicable state laws.

D. Notify all consumers who (1) have purchased any warranted product manufactured between July 4, 1975 and the effective date of the order, manufactured by respondent, and (2) received a warranty which does not comply with the Warranty Act and the Disclosure Rule as stated in the complaint, by mailing to each such consumer the notice set forth in Appendix B of this complaint and order. Respondent shall obtain the names and addresses of such consumers from the warranty coupons which have been mailed to respondent by buyers of respondent's products. In the event that respondent does not have the names and addresses of all such affected consumers, respondent shall contact all retail outlets which sell respondent's products and use every means possible, including securing copies of sales invoices in the possession of such retailers, to obtain the names and addresses.

E. Notify, within 30 days from the effective date of the order, all its dealers who sell respondent's mobile homes, and all its agents and employees who are authorized to handle warranty claims, of all changes in its written warranties, including, but not limited to consumer rights and remedies available to them under the warranty and this order.

F. Notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any change in the corporation which may affect compliance obligations arising out of the Order.

G. Deliver a copy of this order to cease and desist to all present and future employees, salesmen, agents, independent contractors and other representatives engaged in the preparation and distribution of written warranties and in the sale of warranted consumer products on behalf of respondent, and secure a signed statement acknowledging receipt of the order from each such person.

H. Maintain, for a period of three (3) years from the effective date of the order, complete business records of the manner and form of respondent's continuing compliance with all the terms and provisions of the order, to be furnished upon request to the staff of the Federal Trade Commission during normal business hours and upon reasonable advance notice.

I. Shall within sixty (60) days after service upon it of this order, file with the Commission a report in writing, setting forth in detail the manner and form in which it has complied with this order.

APPENDIX B

[Name and Address of Consumer] [Date]

Dear [Name of Consumer]:

You have some added warranty protection for your mobile home. The Federal Trade Commission has told us to write you about it.

The warranty you got says you have no implied warranties under state law. This isn't so. You have these warranties, for at least four years from the date of purchase.

First, you have a warranty of "merchantability." This means your home must be in livable condition.

Second, you may have a warranty of "fitness for a special purpose." If, when you bought your home, you relied on our advice or our ads that it was fit for a special purpose, it must live up to that promise.

If your home doesn't live up to one of these warranties, and we can't make it do so, you may have a legal right to cancel your purchase and make a claim for some of your money back. If you feel this is the case, please contact your dealer, or call us collect at (telephone number).

However, we will not be responsible for fixing any damage caused by your misuse or abuse of the home, or by such uncontrollable forces as lightning, floods, and the like.

Our warranty also said you had to send us your registration card. Again, this isn't so. We'll accept any reasonable proof of purchase or delivery date. A sales slip or receipt will be okay.

Also, our warranty said we will not pay for any incidental or consequential losses caused by a manufacturing defect in the product. We want you to know that in some cases, and in some states, even these are covered.

Please excuse these mistakes in our warranty.

Sincerely,

Madison Mobile-Modular Homes, Inc.

FTC Dkt. C-2973, June 21, 1979.

IN THE MATTER OF

MOTHERHOOD MATERNITY SHOPS, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2974. Complaint, June 21, 1979 — Decision, June 21, 1979

This consent order, among other things, requires a Santa Monica, Calif. manufacturer and seller of maternity wearing apparel and related products and its corporate owner to cease establishing, maintaining and enforcing resale prices and sale periods for their products; soliciting, exchanging or disseminating price information; and compelling adherence to such prices and sale periods through persuasion or coercion. Respondents are additionally prohibited from withholding advertising allowances, or otherwise taking adverse action against recalcitrant retailers.

Appearances

For the Commission: *Sandra L. Bird* and *Elliot Feinberg.*

For the respondents: *George Zachary, Rosenfeld, Meyer & Susman,* Beverly Hills, Calif.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Motherhood Maternity Shops, Inc., a corporation, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Motherhood Maternity Shops, Inc. (hereinafter sometimes referred to as Maternity Shops) is a corporation organized, existing and doing business under and by virtue of the laws of the State of California with its principal office and place of business at 1330 Colorado Ave., Santa Monica, California.

PAR. 2. Respondent MMS of Delaware, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 1330 Colorado Ave., Santa Monica, California.

MMS of Delaware, Inc. acquired all of the stock of Motherhood Maternity Shops, Inc. in July 1977, through the merger of Motherhood Maternity Shops, Inc. and MMS of California, Inc., a wholly-owned subsidiary of MMS of Delaware, Inc.

PAR. 3. Respondent Maternity Shops is now, and has been, engaged

(2) advertising a product at a price other than that which respondent Maternity Shops has established or suggested.

PAR. 9. The acts, practices and methods of competition engaged in, followed, pursued or adopted by respondent, as hereinabove alleged, are unfair methods of competition and unfair acts or practices because they have the tendency to, or the actual effect of:

(a) fixing, maintaining or stabilizing the prices at which respondent Maternity Shops' products were resold;
(b) suppressing or eliminating price competition between or among resellers selling respondent Maternity Shops' products and between such resellers and respondent Maternity Shops; and
(c) depriving consumers of the benefits of competition.

PAR. 10. The aforesaid acts, practices and methods of competition, constitute unfair methods of competition and unfair acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of the complaint which the New York Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act, as amended; and

The respondents, their attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it has reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Motherhood Maternity Shops, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of California with its office and principal place of business located at 1330 Colorado Ave., Santa Monica, California.

Respondent MMS of Delaware, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its office and principal place of business located at 1330 Colorado Ave., Santa Monica, California. Respondent Motherhood Maternity Shops, Inc. has been merged with MMS of California, Inc., a wholly-owned subsidiary of MMS of Delaware, Inc. The surviving corporation, Motherhood Maternity Shops, Inc., is a wholly-owned subsidiary of MMS of Delaware, Inc.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

Order

For purposes of this order, the following definitions shall apply:

"Product" is defined as any item of wearing apparel and any related accessory and any other merchandise, service or thing which is manufactured, offered for sale, or sold by respondents or any of their subsidiaries.

"Reseller" is defined as any corporation, firm or person which sells or which requests to sell any product sold or distributed by respondents or any corporation or firm owned or operated by respondents, but excluding persons, partnerships or corporations operating retail outlets owned or operated by respondents or any of their subsidiaries.

"Resale price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula, or margin of profit used by any reseller for pricing respondents' products. Such term includes but is not limited to any suggested, established or customary resale price as well as the retail price in effect for retail outlets or departments owned or operated by respondents or any of their subsidiaries.

"Sale period" is defined as any time period during which retail outlets or departments owned or operated by respondents or any of their subsidiaries offer any product for sale at resale prices lower than those in effect during the usual and ordinary course of business; or any suggested, authorized or customary time for selling or advertising apparel at prices lower than suggested, established or customary resale prices.

"Company-owned store" is defined as any retail outlet owned or operated by respondents or any of their subsidiaries.

I

It is ordered, That respondents Motherhood Maternity Shops, Inc., a corporation, and MMS of Delaware, Inc., a corporation, their successors and assigns, and respondents' officers, their agents, representatives and employees, directly or indirectly, or through any corporation, subsidiary, division or other device, in connection with the manufacture, offering for sale, sale, distributing or advertising of any product in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, shall forthwith cease and desist from:

1. Fixing, establishing, controlling, stabilizing, maintaining or enforcing, directly or indirectly, the price at which any reseller may advertise, promote, offer for sale or sell any product.
2. Establishing, exacting assurances to comply with, continuing or enforcing any contract, agreement, understanding or arrangement with any reseller to fix, establish, control, stabilize, maintain or enforce, directly or indirectly, the price at which any product is to be resold or advertised.
3. Establishing, exacting assurances to comply with, continuing or enforcing any contract, agreement, understanding or arrangement with any reseller to tie any resale price of any reseller to any resale price in effect at any company-owned store.
4. Suggesting, communicating, publishing, disseminating, circulating or providing by any means any information concerning resale prices or sale periods to any reseller. The advertising to consumers of actual resale prices by any company-owned store shall not be deemed as violation of this paragraph.
5. Soliciting, gathering or exchanging, directly or indirectly, information concerning any resale price or sale period of any reseller.
6. Establishing, exacting assurances to comply with, continuing or enforcing any contract, agreement, understanding or arrangement with any reseller to fix, establish or control the form, content or timing of the advertising of any product by any reseller.
7. Suggesting, recommending, advising, persuading, inducing or coercing any reseller to establish, maintain, issue, adopt or adhere to

any resale price, or to establish, maintain, issue, adopt or adhere to any sale period.

8. Communicating with any reseller concerning any deviation or alleged deviation from any resale price or sale period.

9. Suggesting, recommending, advising, persuading, inducing or coercing any reseller to refrain from or to discontinue advertising any product at a certain resale price.

10. Representing directly or by implication that any action may or will be taken against any reseller who deviates from any resale price or sale period.

11. Securing or attempting to secure any promise or assurance from any reseller regarding the price at which such reseller will or may advertise or sell any product; or requesting or requiring any reseller to obtain approval from respondents for any price at which such reseller may or will advertise or sell any product.

12. Threatening to withhold or withholding advertising allowances or any other assistance, payment, service or consideration from any reseller, or limiting or restricting eligibility of any reseller to receive such benefits because said reseller advertises or sells any product at certain resale prices.

13. Taking any action to hinder or preclude the lawful use by any reseller of any trademark of any respondent in conjunction with the sale or advertising of any product.

14. Terminating, suspending, delaying shipments to, or taking or threatening any action against any reseller because the reseller has, or was alleged to have sold or advertised any product at a certain resale price, or because the reseller may engage in any such activity in the future.

II

It is further ordered, That respondents shall:

1. Within thirty (30) days after the date of service of this order, mail under separate cover a copy of this order to every past reseller. An affidavit of mailing shall be sworn to by an official of respondents verifying that said mailing of this order was completed.

2. Mail a copy of this order to any reseller that purchases any products from respondents within five (5) years after the date of service of this order. The mailing required by this provision shall occur within thirty (30) days after the first purchase by said reseller.

3. Within thirty (30) days after the date of service of this order distribute a copy of this order to each of their operating divisions and subsidiaries and to all officers, supervisory sales personnel, sales

agents and representatives selling to resellers, and to advertising agencies retained by respondents and secure from each entity or person a statement acknowledging receipt of said order.

III

It is further ordered, That respondents:

1. Notify the Commission at least thirty (30) days prior to any proposed change in the respondents such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation of or dissolution of subsidiaries or any other such change in the corporations which may affect compliance obligations arising out of this order.

2. Maintain complete business records which fully disclose the manner and form of respondents' compliance with the Order, including but not limited to any records referring or relating, in whole or in part, to:

(a) any communication between any respondent and any reseller relating to any price at which any reseller, person or firm is selling, proposes to sell, is advertising or proposes to advertise any product;

(b) the termination of any reseller for any reason; or

(c) the refusal to deal with any reseller for any reason.

Respondents shall maintain the records required by this paragraph for at least three (3) years from the date such records were created or received by respondents. The records required by this paragraph shall be made available to Commission staff upon reasonable notice.

3. Within sixty (60) days after service upon them of this order, file with the Commission a report, in writing setting forth in detail the manner and form in which they have complied with this order.

IN THE MATTER OF

CROWN TUFT, INC., ET AL.

Docket C–1192. Interlocutory Order, June 26, 1979

ORDER DENYING MOTION TO MODIFY OR VACATE CONSENT ORDER

By letter dated May 9, 1979 individual respondent Arthur B. E. Lauman petitioned the Federal Trade Commission to reopen the proceeding in the above-docketed matter to vacate the order as it pertains to him as an individual and as it pertains to the named corporation, dissolved sometime after 1971.

Mr. Lauman states that he had "no personal knowledge" of and he did not "condone in any fashion, any of the charges contained within the consent order agreement;" he sold Crown Tuft, Inc. to Johns-Manvillle Corporation in 1968; he was employed by Crown Tuft until 1971; he is "no longer engaged by or associated with either the existing company or the company to which Crown Tuft, Inc. was sold;" to the best of his knowledge, Crown Tuft, Inc. was dissolved and Johns-Manville Corporation "disposed of the carpet division some years ago."

The order issued against the respondents on April 11, 1967 (see 71 F.T.C. 646) forbids them from misbranding textile fiber products and requires them to disclose the names and amount of constituent fibers contained in carpets, on labels, tags, invoices, and advertisements, pursuant to the provisions of the Textile Fiber Products Identification Act and the rules and regulations promulgated thereunder.

It is axiomatic that corporations can only act through individuals, and it is well settled that the Commission may properly name officers, directors, and sole stockholders of corporate respondents in their official as well as their individual capacities in order to prevent the evasion of its order. *F.T.C.* v. *Standard Education Society,* 86 F.2d 692 (2d Cir. 1936), *rev'd. on other grounds,* 302 U.S. 112, 120 (1937); *Abel Allan Goodman* v. *F.T.C.,* 211 F.2d 7, 14–15 (2d Cir. 1954). The purpose of doing so is to make the order fully effective in preventing recurrence of the practices found to be unlawful, for the Commission has recognized that a corporate respondent is not the only vehicle through which individuals, who have been personally involved in unlawful practices, may in the future continue to engage in such practices. *Tractor Training Service* v. *F.T.C.,* 227 F.2d 420, 425 (9th Cir. 1955), *cert. denied,* 350 U.S. 1005 (1956); *Consumer Sales Corp.,* v. *F.T.C.,* 198 F.2d 404, 407–408 (2d Cir. 1952), *cert. denied,* 344 U.S. 912

(1953). The U.S. Court of Appeals for the Fourth Circuit stated in *Pati-Port, Inc.* v. *F.T.C.*, 313 F.2d 103, 105 (1963):

> . . .it would seem in cases of this sort to be a futile gesture to issue an order directed to the lifeless entity of a corporation while exempting from its operation the living individuals who were responsible for the illegal practices.

There was, accordingly, no miscarriage of justice in making the order effective against individual respondent Lauman, and there is no overriding public interest in vacating the order now.

Where the illegal practice is capable of being resumed, the Commission may take measures to prevent any possible invasion of its orders, even upon a showing that the corporation has been dissolved, and that the named individual has not been for several years and is not now engaged in the sale of carpets.

Petitioner has not set forth any changed condition of fact or law in support of his request, nor has he advanced any argument to demonstrate how the public interest would be served by setting aside this order. Accordingly, the petition is hereby denied.

Revocation of Advisory Opinion issued to Don Odessky, Inc., 87 F.T.C. 1426. [*File No. 763 7002, Don Odessky, Inc.*]

Letter Denying Stay of Revocation

January 22, 1979

Dear Mr. Meisburg:

This responds to your letter of January 16, 1979, on behalf of Don Odessky, Inc., requesting an immediate stay of the Commission's order of January 11, 1979 revoking its advisory opinion in the above-referenced matter and publication of that order.

Having given careful consideration to your request, the Commission has determined that it should be denied. The request advances no basis on which the revocation should be reconsidered, and the Commission is aware of none. Moreover, the Commission is of the opinion that its revocation is a discretionary act not subject to review in the Court of Appeals or otherwise. See 15 U.S.C. Section 45(c); *Florsheim* v. *Engman*, 494 F.2d 949 (D.C. Cir. 1973). In addition, the Commission believes that a delay in publication would be contrary to the public interest in promptly informing the public of its official acts.

By direction of the Commission.

Revocation Letter

January 11, 1979

Dear Mr. Meisburg:

On January 27, 1976, the Commission issued to Don Odessky, Inc., an advisory opinion concerning a tripartite promotional assistance plan, featuring aisle-end displays.[1] The Commission conditioned this advisory opinion on the following reporting requirement:

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[1] 85 F.T.C. 1426.

> To assure that the plan is implemented so as to provide allowances to all competing purchasers on proportionally equal terms, Don Odessky, Inc., should report to the Commission, after the plan has been in operation for one year, the full extent of retailer and supplier participation, including time periods and products involved, and the total allowances paid to each participating retailer by each supplier under the plan.[2]

Pursuant to this reporting requirement, on March 3, 1977, the Commission received a submission from Don Odessky, Inc.

The Commission has determined that this submission failed to disclose "the full extent of retailer and supplier participation," "the time periods and products involved," and "the total allowances paid to each participating retailer by each supplier under the plan." Based on the information provided, therefore, the Commission is unable to determine whether competing purchasers receive payments under the program on equal terms.

Due to the failure and refusal of Don Odessky, Inc., to comply with the reporting requirements of the Commission's opinion, the Commission has decided to revoke the advisory opinion. By this action, the Commission's advisory opinion to Don Odessky, Inc. is rendered null and void. After the date of service of this letter, representations by Don Odessky, Inc. that the Federal Trade Commission in any manner condones or approves any business proposal by that firm would be deceptive and untrue, and could result in such further action by the Commission as would be in the public interst.

By direction of the Commission.

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[2] *Id.* at 1427.

Proposed statistical reporting program entailing the forecasting of annual sales and captive use of selected thermoplastic resins. [*793 7002, Society of the Plastics Industry, Inc.*]

May 1, 1979

Dear Mr. Bercovici:

This responds to your request for an advisory opinion on the use by the Society of the Plastics Industry (SPI) of a proposed statistical reporting program entailing the forecasting of annual sales and captive use of selected thermoplastic resins.

The Commission understands that SPI is a trade association with membership open to all firms in the industry upon payment of annual dues graduated according to sales volume, and that current membership accounts for approximately 95% of the total domestic production of plastics raw materials. The Commission further understands that under the proposed program, resin suppliers would be invited to report their respective forecasts for the current year and each of the following four years to an independent accounting firm, which would compute the mean and median of the reported forecasts and publish the low forecast, the high forecast, the mean, and the median (not broken down by type or grade). There would be no exchange or disclosure whatever of individual firm data and no narrative or interpretation will be placed on the compiled figures. Nonmember producers would be invited to participate in the program on the same basis as members and will receive copies of the forecasts. The reports would also be available by subscription to the public after a trial period. No forecast would be reported, however, unless at least four industry members, excluding any firm with more than 65% of any reporting category, submit forecasts. Initially, the program would encompass six of the major plastics materials: polyvinyl chloride (PVC); low density polyethylene (LDPE); high density polyethylene (HDPE); polypropylene; polystyrene; and acrylonitrile-butadiene-styrene (ABS).

Some types of forecast arrangements among competitors do raise serious antitrust concerns in particular market environments. On the basis of available information concerning the slowing rate of growth, the degree of concentration, the relatively small number of firms engaged in the manufacture of the individual thermoplastic resins, and the specifics of the proposed plan, the Commission is of the view that there is a significant risk that SPI's program could be used to foster an anticompetitive consensus on production levels. The Commission is therefore unable to approve use of the proposed statistical reporting program.

By direction of the Commission.

Letter of Request

January 31, 1978

Dear Mr. Thomas:

On behalf of the Committee on Resin Statistics of the Society of the Plastics Industry, Inc., we respectfully request that the Commission issue an advisory opinion, pursuant to Section 1.1 of its rules of General Procedures, concerning the statistical program described below which the Committee contemplates implementing in 1978.

The Society of the Plastics Industry, Inc. (SPI), is the major national trade association of the plastics industry. It is comprised of more than 1200 member companies which supply raw materials, fabricate manufactured plastics components and products, engineer or construct molds or similar accessory equipment for the plastics industry, and engage in the manufacture of machinery used to make plastic products or materials of all types. Its membership is responsible for an estimated 95% of the total production of some 27 billion pounds of plastics raw materials in this country.

The Committee on Resin Statistics (CRS) is one of 52 operating units of SPI. The Committee is charged with the responsibility to develop meaningful, timely and accurate statistics concerning plastic resins for use by members of the industry, government agencies and other interested parties. The Committee also gathers information from other trade sources and government sources and compiles and publishes an annual volume of "Facts & Figures of the Plastics Industry". A copy of the 1977 edition of "Facts and Figures" is associated herewith.

The CRS presently conducts statistical programs for approximately forty specific plastics materials or groups of plastics materials.[1]

[1] The following major materials are included in the CRS programs:

Epoxy, polyester, urea	engineering and specialty plastics
melamine, phenolic	isocyanates

(footnote continued)

For each of these materials, data is compiled and reported describing both Production and Sales & (Captive) Use, in reporting units based upon weight. Reports are compiled on a monthly, quarterly, semi-annual or annual basis, depending upon the specific materials or group of materials involved. Additionally, for certain of these materials, data is compiled and reported concerning inventory, capacity and/or total dollar value of sales. All present statistical programs report the historical experience pertaining to the included materials.[2]

The Committee on Resin Statistics is presently contemplating, and by this letter requests the Commission's advice concerning, the institution of a statistical reporting program entailing forecasting of annual sales and captive use of selected plastic resins. Such a program is not presently being conductd by CRS; and the institution of such a program, entailing forecasting rather than the reporting of historical data, would represent a departure from current practice.

To develop the proposed annual sales forecast, members of the industry will be requested to voluntarily submit their best estimates of *total* United States demand for plastic resins, i.e., the category presently indentified as Sales & Use in SPI's statistical reports.[3] Demand would be forecast in thousands of pounds, for the then-current year and for each of the next four years, for each of the materials the company produces which is included in the program. The data collected and compiled will thus be projected total demand, not directly influenced by such proprietary information as the reporting companies' corporate planning with respect to expanded or constricted production, new marketing programs, etc.

(continued from previous page)

- low density polyethylene
- high density polyethylene
- polypropylene
- ABS
- SAN
- polystyrene
- nylon
- polyvinyl acetate
- polyols
- polyurethane products
- styrene butadiene latexes
- other styrene-based latexes
- other styrene-based polymers
- PVC
- polyvinyl alcohol
- other vinyl resins

[2] One minor variant is that capacity figures are reported annually on the basis of capacity both as of December 31 of the year just ended and also as adjusted to December 31 of the current year, with the latter figure incorporating publicly announced plant expansions or contractions.

[3] The "use" element of the Sales & Use category pertains to internal consumption by the resin producer.

The individual company figures will be directly submitted to Ernst & Ernst, the independent public accountants which presently serve all of the CRS statistical programs. Ernst & Ernst will compile and distribute the reports, showning the high and low forecasts and the mean and median averages. There will be no narrative or interpretation placed upon the compiled figures; nor will the reported figures disclose the identity of the participants responsible for the specific forecasts. Moreover, in accordance with the "disclosure" rules governing the CRS programs, no figures will be reported unless there is participation by at least four members of the industry, no one of which is so dominant as to represent more than 65% of any reporting category. Additionally, according to CRS policy for this proposed program, in order to assure that the forecasts represent a valid cross-section of the industry, no program will proceed unless a minimum percent of the present producers participate in the report for each material. That minimum participation, originally established at 70%, is subject to revision. Furthermore, these reports would be available by subscription to the general public, as are other CRS reports.[4] Copies of the draft reporting instructions and format for dissemination of the compiled information are also associated herewith.

Initially, the annual sales forecasting program will encompass six of the major plastics materials. Those materials, and the present volume (sales & use) and number of producers are, as follows:

Material	Sales & Use[5] (millions of lbs.)	Number of Producers[5]
polyvinyl chloride	4,638	21
low denisty polyethylene	5,765	14
high density polyethylene	3,127	14
polypropylene	2,536	10
polystyrene	3,145	19
acrylonitrile-butadene-styrene (ABS)	925	7

Other materials may be added at a later date.

[4]As with any newly instituted reporting program, reports are not placed on subscription availability until completion of an initial "shake-down" period, generally one or two reporting periods, to allow evaluation of reporting instructions, etc.

[5]Source: Facts and Figures of the Plastics Industry—1977 Edition, The Society of the Plastics Industry, Inc., New York, 1977. Further information concerning these and other plastics materials is contained in the associated copy of Facts and Figures.

The Committee on Resin Statistics foresees substantial benefits flowing from its proposed annual sales and use forecasting survey. Presently there is no source of information of this nature available on a continuous and credible basis. It is understood that consultants have prepared demand forecasts for plastic resins. These reports, however, are sporadic rather than periodic, limited to the sponsors or subscribers and not generally available to the public, and quite expensive. Moreover, in that the forecasting techniques utilized by the consulting firms for such reports are not disclosed, there is no basis for confidence in the reports or comparability among such reports.

From an industry standpoint, the availability of this data may assist the resin producers to better define the capacity needs of the plastics industry by improving upon their understanding of market demand. Fabricators of component or finished plastic products, including users such as the automotive industry, may better be able to plan for their future materials (resins) supplies and requirements by better understanding total projected industry demand *vis-a-vis* present production capacity. Similarly, such projections will assist suppliers to the industry of equipment such as processing (fabricating) machinery, hopper cars, storage silos, conveyers, etc., to plan to serve the future requirements of the plastics industry. Improvement in the long range planning capability is beneficial and desirable in view of the long lead time between planning and start-up of new production facilities and should thereby improve the efficiency at all levels of the supplier, consumer and allied industries.

In addition, to the potential benefits to the plastics industry and its suppliers, the availability of projected demand for plastics resins will be of assistance to those departments and agencies of the Federal Government having responsibility for planning for future energy requirements. Such data will assist with respect to planning for both the consumptive use of energy in the production of plastics materials and products and the productive use of energy in that plastics materials are derivatives of petroleum products. In the event of future critical shortages of petroleum products, such data will assist with respect to the impact analysis pertaining to matters such as feedstock allocation and energy allocation, to the extent that such measures may be necessary. Such forecasts will also be of benefit with respect to projecting future employment levels within the industry and of assistance to the financial community in analyzing the long range prospects of the chemical and plastics industries.

As hereinbefore described, the contemplated course of conduct described herein is not presently being followed by SPI's Committee on Resin Statistics; nor, to the knowledge and information of the staff and officers of the Committee, is such course of conduct being followed by other operating units of SPI. Additionally, neither the Committee staff nor officers are aware of any pending investigation or other proceeding by the Commission or any other governmental agency concerning the matter described herein.

The Committee on Resin Statistics of the Society of the Plastics Industry, Inc., respectfully requests the advice and comments of the Federal Trade Commission with respect to the conduct of the annual sales forecasting program described herein. Any questions concerning the program described herein or any requests for further information necessary for the Commission to reach a conclusion with respect to this matter may be directed to the undersigned.

Respectfully submitted,

/s/ *Martin W. Bercovici*

Assistant General Counsel to
The Society of the Plastics
Industry, Inc.

Second Letter of Request

May 25, 1978

Dear Mr. Garvey:

We are pleased to respond to your inquiry dated April 26, 1978, requesting clarification with respect to the Request for Advisory Opinion submitted to the Commission on behalf of the Committee on Resin Statistics of the The Society of the Plastics Industry, Inc., pertaining to a proposed statistical reporting program entailing forecasting of annual sales and use of selected plastic resins. The specific issues raised in your letter are addressed, as follows:

(1) Sales and captive use will be the only data which will be collected in the proposed forecasting program.

(2) In essence, sales and captive use is the same as production plus or minus adjustments to inventory.* Variances of a minor nature may occur between production and inventory adjustments on the one hand and sales and captive use on the other due to such factors as product loss which may occur in packaging operations or due to contamination; however, the Committee on Resin Statistics does not address such factors in its statistical programs. The sales and captive use terminology has been employed by the Committee simply as a convenient means of collecting statistical data due to the commonality of the use of these measurements among the various companies. One reason for this is that the six categories of plastic materials which will be encompassed within this program are manufactured in a continuous process, rather than in a batch process. Accordingly, the figures for sales and captive use are more precise than the statistics measuring production itself.

(3) In forecasts of future sales and captive use, it is not anticipated that adjustment for future inventory will be a material consideration. Inventory adjustments are the net differential between production (and imports) on the one hand and sales and captive use on the other; and the objective of the proposed program is to forecast trends in sales and captive use (i.e., demand) rather than production.

(4) The term "demand" as used in our request of January 31 is intended merely as another term for sales and captive use. Other than being added to inventory, plastic resins either may be sold by the producers to fabricators or to other parties (e.g., exporters, compounders), or said resins may be used by the producers in captive fabrication operations. Thus, sales and captive use together describe the demand for the particular resins. Demand relates to supply from the standpoint of the latter entailing the availability of plastic resins to meet the demand through production and inventory.

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*The program as planned is based solely on domestically produced resins and thereby excludes imports. Sales of imported materials may, however, cause a minor variance in a comparison of sales and captive use v. production and inventory adjustments. At present, imports of plastics resins are not a significant factor in the domestic market.

(5) The proposed statistical program will entail the collection of data on projected sales and captive use, i.e, demand projections, from resin suppliers only rather than from fabricators. Consistent with the underlying goal of the Committee in the conduct of all programs to develop as complete and meaningful data as possible, non-members of The Society which produce plastic resins will be invited to participate in this program on the same basis as member companies.

(6) SPI has no specific knowledge of the techniques utilized by the resin producers to prepare market forecasts for their own internal corporate purposes; however, it has no reason to believe that data projections as contemplated by the proposed program are presently collected from customers by producers of the six designated plastics raw materials. It is not contemplated that producers will seek such information from their customers as part of the proposed program.

(7) Based upon available statistics, such as the Census of Manufacture published by the Department of Commerce, it is believed that there are approximately 25,000 establishments which fabricate plastic products in the United States. These firms run the gamut in size from very small individual proprietorships to multi-national corporations; and they vary from those which engage solely in plastics fabrications operations to those which fabricate component parts for assembly in goods manufactured of other materials to those which employ relatively small amounts of liquid plastic resin as a binder or other component of manufacture of various products (e.g., paint, fiberglass, etc.). Of these approximately 25,000 establishments, probably less than 5%, numerically, belong to The Society of the Plastics Industry, Inc. Accordingly, forecasting demand on the basis of sampling or other survey techniques would be quite expensive and time consuming and may or may not lead to valid results. On the other hand, the Committee on Resin Statistics believes the producers are in an adequate position to furnish this information. Through their requirements for remaining alert to economic conditions, socio-economic considerations (e.g., increased use of plastics to less automobile weight to conserve gasoline), product innovation and other factors similarly af-

fecting demand, it is believed that the producers, by the contemplated consensus procedure, will be able to meaningfully forecast trends and future demand requirements.

(8) Under the proposed program, suppliers will forecast total market demand for the materials which they produce. This projection will be unrelated to the individual producer's plans relating to each company's position as a supplier in the market. For example, a supplier's position may be related to its plant capacity, the level of plant capacity at which the producer operates, its plans and capability for expansion of plant capacity, its supply of feedstocks, its alternate use of those feedstocks, its desire to grow—or even continue to serve—an individual resins market, and its plans and ability to switch production from one resin to another. For the foregoing factors, and considering the procedures to govern the conduct of the program, the Committee believes that individual projections of position will not enter into the data the respondents are requested to furnish.

(9) The reporting instructions, a draft of which was associated with our request of January 31, do not address the manner in which the respondents will prepare their projections. Accordingly, and consistent with the response to item number 8 above, the answer to item 9 is that the nature of the influence of the described information will not be direct.

(10) With respect to the benefits to be derived from the program, the Committee on Resin Statistics desires to develop meaningful data so that producers, fabricators, users, equipment suppliers, etc., may individually develop better insights into the marketplace to improve future planning by having the benefit of the collective judgment of the supplier industry as to the potential future of each resin segment. The interpretation and use of the information will be at the sole discretion and judgment of each interested party. Inasmuch as the proposed program will be one source of information, among many, it is believed that the influence of the described information on individual decision-making will not be direct.

We trust the foregoing is responsive to your inquiry. Should you have further questions or desire further information or elaboration, please feel free to contact the undersigned.

Cordially yours,

/s/ Martin Bercovici

Third Letter of Request

September 6, 1978

Dear Ms. Melman:

This will serve to respond to your recent request for additional data relative to the request for Advisory Opinion we submitted to the Commission on behalf of the Committee on Resin Statistics of the Society of the Plastics Industry, Inc., dated January 31, 1978.

Associated herewith, please find production data for the year 1977 for the six categories of plastics materials encompassed within the contemplated forecasting program. This data is derived from the statistical program conducted by the Committee on Resin Statistics as compiled by Ernst & Ernst. Secondly, we are enclosing abstracts from prior editions of "Facts & Figures of the Plastics Industry" showing estimated capacity, by product and manufacturer, as of January 1, 1973-76. 1973 was the first year of publication of "Facts & Figures" and therefore is the earliest such figures are available. The estimated capacity by manufacturer for 1977 is shown in the 1977 edition of "Facts & Figures," copies of which were submitted with the January 31 request. Additionally, the estimated capacity figures to be published in the 1978 edition of "Facts & Figures" are also enclosed. Please note that the 1978 edition will reflect estimated capacity as of December 31 of the year just ended rather than January 1 of the year of the edition of the "Facts & Figures" publication.

With respect to the capacity information, please note that total capacity, by material, is derived from the Committee's annual survey of capacity compiled by Ernst & Ernst. The figures shown for capacity by individual manufacturing company are derived from publically available sources, such as corporate annual reports, corporate news and publicity releases, trade magazines and other like sources. Any differential between the sum total of the estimated capacity by individual manufacturers and the total as derived through the Committee's statistical program is reconciled by the SPI staff through "guestimated" adjustments to the figures shown for the individual companies. Such a reconciliation procedure is necessary inasmuch as the Committee's statistical programs are conducted on a confidential basis, with all data being reported to Ernst & Ernst, the SPI staff having no access to such data.

We trust the foregoing is responsive to your request. In the event that further information may be required, please feel free to communicate with the undersigned.

Very truly yours,

/s/ *Martin Bercovici*

TABLE OF COMMODITIES*

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