SCOPE OF FEDERAL TRADE COMMISSION ORDERS IN PRICE DISCRIMINATION CASES

By

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I embrace the opportunity to discuss one of the Federal Trade Commission's most difficult problems before this informed group. I am honored to share the platform with Edgar Barton, to whose keen mind and persuasive presence I am no stranger. In fact, we have recently exchanged ideas on this very subject before a different forum—the Court of Appeals for the Seventh Circuit.

Before getting on with the subject, I must say a word about my limitations. As an employee of the Commission, I am not authorized to speak for it. The point of view and opinions that I express will be my own and not necessarily those of the Commission. Moreover, as the discussion deals with a field in which the law is still developing, there might be some temptation to discuss and analyze real cases and to plug the Commission's position in them. I shall carefully avoid that temptation and address myself generally to the problems the Commission faces in formulating cease and desist orders in price discrimination cases. Furthermore, I shall avoid discussing the terms of any specific order, as the myriad factors involved in any one situation cannot be examined with sufficient care and objectivity in this kind of meeting.

I think I can best serve your interests if I try to indicate the nature and variety of the problems encountered in drafting orders that are effective from the point of view of the public interest, fair to the respondents involved and to their competitors, and at the same time in accord with economic realities. In doing so, I do not mean to suggest that I have all the answers or that the Commission has solved all of the problems.

However, we *can* begin with some pretty well-settled principles in mind.

There is a large body of existing law on the general subject of drafting orders—

These precedents and principles are derived from the efforts of district courts and other government agencies to draft orders. While those sources will provide us with valuable background, I am dealing today with problems that are peculiar to the Federal Trade Commission. For that reason I shall confine my discussion to Commission cases which are our guideposts in approaching the problems presented by specific situations. In this connection I am thinking particularly

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about such cases as: *Hershey Chocolate*,[1] *Jacob Siegel*,[2] *Morton Salt*,[3] *Ruberoid*,[4] *National Lead*[5] and *Niehoff* cases.[6]

I look upon the *Hershey Chocolate* case as standing for the proposition that an order should not be limited to proscribing the specific acts by which the violation was manifested but that, to be of any value, it must also forbid the unlawful method employed. In this particular case the court approved an order inhibiting unfair practices in connection with several different confectionery items even though the complaint was limited to one item.

The *Jacob Siegel* case stands for the proposition that the Commission, as an expert body, has wide latitude in fashioning its orders and the courts will not interfere except where the remedy selected has no reasonable relationship to the unlawful practices found to exist.

In the *Morton Salt* case the Supreme Court disapproved a Commission price discrimination order containing provisos permitting certain price differentials "if they do not tend to lessen, injure or destroy competition." I look upon this case as standing for the proposition that the Commission may not shift to the courts the job of determining whether or not a particular price difference may have the effect prohibited by the statute.

The *Ruberoid* case is the most significant touchstone of them all. There the Supreme Court reaffirmed the principles of the *Hershey* and *Siegel* cases as specifically applied to a price discrimination situation. The Court emphasized that the purpose of Commission orders is to prevent illegal practices in the future. It said that—

> "In carrying out this function the Commission is not limited to prohibiting the illegal practice in the precise form in which it is found to have existed in the past. If the Commission is to attain the objectives Congress envisioned, it cannot be required to confine its road block to the narrow lane the transgressor has traveled; it must be allowed effectively to close all roads to the prohibited goal, so that its order may not be by-passed with impunity."

The particular discriminations charged in the *Ruberoid* complaint arose from a system of customer classification, but the Supreme Court approved a broad-scale order prohibiting discrimination between competing customers of the seller. The Court also held that "cost justification" and "good-faith-meeting" provisos were not a necessary part of an order. This is so, it said, because, even if they are not stated, the provisos are necessarily implicit in every order issued under the Act.

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1. *Hershey Chocolate Corp.* v. *Federal Trade Commission*, 121 F. 2d 968 (C. A. 3, 1941).
2. *Jacob Siegel Co.* v. *Federal Trade Commission*, 327 U. S. 608 (1946).
3. *Federal Trade Commission* v. *Morton Salt Co.*, 334 U. S. 37 (1948).
4. *Ruberoid Co.* v. *Federal Trade Commission*, 343 U. S. 470 (1952).
5. *Federal Trade Commission* v. *National Lead Co.*, 352 U. S. 419 (1957).
6. *Federal Trade Commission v. C. E. Niehoff & Co.*, 355 U. S. 941 (1958).

The *National Lead* case is perhaps most important from the point of view of conspiracy orders, but it again reaffirms the *Siegel* doctrine that the Commission's judgment in fashioning orders is not to be interfered with unless it is arbitrary or clearly wrong.

The *Niehoff* case, which is of very recent vintage, held that it is for the Commission to decide whether its order against one member of an industry ought to be held in abeyance until the Commission has also proceeded against other members of the industry. This case focuses attention upon the possibility that in some types of situations the Commission might find it advisable to set the effective dates of orders so as to avoid putting any particular member of an industry at a competitive disadvantage.

Starting from those general principles, the Commission must fashion orders that are responsive to a wide variety of situations.

Price discriminations, of course, all involve different prices charged different buyers from the same seller. The cases, however, are conventionally classified according to the economic interest that suffers by reason of the discrimination. If a competitor of the seller is injured, we have a primary line case, whereas if one of two competing customers of the seller is injured, that is a secondary line case. Each of these categories requires a different type of order and, for that reason, I shall discuss them separately.

Secondary line cases take many forms, depending upon how the discrimination is effected. Some discriminations, for example, arise from annual volume rebate systems or other discounting practices, others arise out of the seller's classification of its customers, and still others from unequal terms of sale. In some other cases, however, the discriminations are not a part of a particular system but are merely aberrations of essentially sound, non-discriminatory pricing methods. Each of these, of course, suggests a peculiar sort of problem in order drafting.

One principle is clear—where the respondent has employed a general system of discrimination, whether by use of quantity discounts, or customer classification, or variable terms of sale, or some other method, the Commission's order will not be limited to merely inhibit that particular method in the future. This is the teaching of the *Ruberoid* case and it is a primary principle of drafting effective orders in this field. The reason is plain. For example, if a seller discriminated by using a quantity discount system and the order prohibited only that system, it could be evaded easily. All the seller would need do would be to shift to a customer classification system that would accomplish the same discrimination but would not violate the order. In such event the Commission would be in the position of having won a law suit and lost a cause.

Sound administration requires that the Commission in fashioning its road block, anticipate that the respondent may in the future use different means to the prohibited goal.

I fully appreciate that Justice Jackson, dissenting in the *Ruberoid* case, took the Commission to task for not fashioning an order more clearly responsive to the facts of that case. We at the Commission were most interested in his remarks but while I have read and reread that well-written dissenting opinion, I have failed to find that he offered any solution. He highlighted one of the basic problems involved in drafting price discrimination orders, but came no nearer solving the problem than I am coming tonight. Respondents claim time and again that the Commission's order merely prohibits what the statute already forbids: that the statute says "Don't discriminate;" the Commission's order, in effect, merely repeating that injunction. But experience has demonstrated that we cannot confine our orders to the particular system from which the price discriminations in question arose without inviting evasion and another law suit.

While it is true that many of our orders broadly inhibit discriminations, there are also many situations in which the Commission is able to confine its road block more narrowly and still have an effective order. This is particularly the case when the statutory violation has not been effected through a systematic method of discrimination, but rather is an aberration of a legal and non-discriminatory price structure. Typical examples of this are the *Auto Safety Glass* cases.[7] Each of the two largest sellers of auto safety glass was charged with discriminating in favor of one of the two largest manufacturers of automobiles, but no other price discrimination was charged. The order in each case merely prohibited discrimination in favor of the auto manufacturer in the sale of safety glass to be used for replacement purposes. In those cases it was possible to write an order responsive to a narrow and specialized factual situation because no other potential discrimination was evident.

Another problem that frequently presents itself is the breadth of the product line which properly should be covered by an order. The most persuasive authority in this field is the *Hershey Chocolate* case. There it was held that a company manufacturing a broad line of chocolate items could be restrained from violating the law in relation to its entire line, even though its illegal practices had extended only to a portion of the line. The key to this decision and my reasoning on this problem is to be found in the relationship between the various items being sold. In the *Hershey Chocolate* situation, the discriminatory pricing system might easily have been extended to cover or substituted to cover similar items not involved in the original proceeding. However, when a seller markets items that are not thus closely related I can generally say that such unrelated items would not likely be covered by an order.

7. *Matter of Libby-Owens-Ford Glass Co.*, F. T. C. Docket 6700 (May 22, 1957), and *Matter of Pittsburgh Plate Glass Co.*, F. T. C. Docket 6699 (April 19, 1957).

I know you are interested in this question of product coverage. Well, frankly, there is no easy answer. Maybe I can explain why that is so with a couple of hypothetical examples.

First, take the relatively simple case of a seller of automotive replacement parts. He is using a discriminatory system to price those parts, but there are a few items that he sells net. Quite obviously they are like or related items and they will be covered by the order.

Now let us complicate this operation a bit more. Assume that the same seller also markets a line of aviation replacement parts. Let us assume further than the Commission's attention has been focused on automotive replacement parts and that there is a reasonable probability of injury arising from the discriminations in the automotive parts replacement line. We know little or nothing about the probability of injury arising in the aviation replacement parts industry. The only thing we know is that the same system is being used in both markets. Now, the question is whether the order should cover both aviation parts and automobile parts or should be limited to automobile parts.

The answer to that question requires more information about the aviation replacement parts market. It might be that sellers are so scattered and non-competitive that the possibility of injury is remote, in which event the order would probably not be extended to the aviation line. Or, on the other hand, market analysis might indicate that injury is likely and, therefore, that the order should also prohibit discriminations in the aviation line.

The ramifications of this problem must be as manifest to you as they are to me. We could complicate the position of our hypothetical manufacturer even further and each time we entered a new complicating factor the problem would become that much more complicated and its solution that much more difficult. No one has ever yet suggested that the Commission knew all the answers and I can tell you frankly that I don't.

The geographic extent of an order, at least in secondary line cases, is a problem that is occasionally raised by the respondent. We do not find this troublesome. We believe that the difficulty usually arises because respondent's counsel misunderstands the nature of Commission proceedings. The usual argument points out that the Commission has proved its case by evidence taken in two or three different cities indicating that a system of price discrimination is being practiced in each of those places. On that basis, respondent's counsel sometimes argues that the Commission's order should not be general in its application, but should prohibit discriminations only in those cities. This is not correct and has no support in case law. The Commission's proof indicates the existence of a system of discriminatory pricing, of which the situation in those cities is merely illustrative. In such circumstances the Commission will prohibit price discrimination on a nationwide basis unless re-

spondent discharges the burden of proving that the discrimination in those areas was only an aberration of a non-discriminatory pricing system.

In any event, Commission orders in the secondary line cases are, at least in one sense, inherently limited in area. This is so because they prohibit price discriminations only between competing customers. Therefore, the area of effectiveness with respect to any pair of competitive customers would be that area in which they compete.

Still another difficult problem that we must consider is that of fairness among the competitors in industries in which all of the sellers or many of them are discriminating among their customers. This problem was dramatically presented in the *Niehoff* case. There the respondent claimed that if an order were issued against it before orders were issued against its competitors, it would be forced out of business. The Commission found that the respondent was violating Section 2(a) of the Clayton Act and refused to delay the effective date of its order. Upon review, however, the Court of Appeals for the Seventh Circuit agreed with Niehoff. It affirmed the Commission's order but held it in abeyance—presumably pending the determination of other price discrimination cases which were then pending against other members of the automotive replacement parts industry.

I had the privilege of presenting the Commission's case before the Supreme Court, which reversed the Second Circuit's decision and directed affirmance of the Commission's order in its entirety. The Court's opinion recognized the broad scope of administrative discretion that Congress has given to the Federal Trade Commission and it pointed out that "in the shaping of its remedies within the framework of regulatory legislation, an agency is call upon to exercise its specialized, experienced judgment." The Court noted the variety of factors which would effect this kind of decision, such for example, as: To what extent is there a relevant industry within which the respondent competes? Is the nature of that competition such as to indicate identical treatment of the entire industry? Does an allegedly illegal practice in fact exist throughout the industry? If so, should all firms in the industry be dealt with in a single proceeding or should they receive individualized treatment? It concluded that "The Commission alone is empowered to develop that enforcement policy best calculated to achieve the ends contemplated by Congress . . ."

Despite the favorable decision in the *Niehoff* case, we at the Commission recognize that the timing of Commission orders in such competitive situations does present a very real problem in many cases. The Supreme Court has held that this is a problem peculiarly within the Commission's special competence. The Commission must examine

each such situation and sometimes strike a balance between the conflicting interests of the consuming public and competitors in the industry. This will not always be an easy task, but it is a necessary one.

Primary line cases are less diverse and less numerous than secondary line cases, but they present an even tougher problem of order drafting. Here we are not concerned with the adverse effects of a price discrimination upon buyers, but rather upon competitors of the seller.

The typical primary line case involves a large seller who injures his smaller competing sellers by discriminating among his own customers. Generally this is accomplished in one of two ways: Either (1) by selectively lowering its prices to certain large purchasers or (2) by lowering its prices in one area while maintaining or increasing them in all other areas.

The *Moss*[8] case is a good example of the first kind of primary line case. There a manufacturer of rubber stamps accorded discriminatory prices to certain of its large purchasers. There was little or no injury to its customers who were charged the higher prices, because rubber stamps constituted a very small fraction of their business. However, there was serious injury to Moss's smaller competitors, because they were unable to compete for the business of the purchasers favored by Moss.

The other type of primary line case is the area price discrimination. Here, typically, a large manufacturer sells its product nationally or at least over a wide geographical area, whereas, in a certain small portion of that area, it has one or more competing sellers. The large manufacturer lowers his price in the area in which it has competition, but maintains or increases its prices elsewhere. The result, economically, is to increase the demand for the seller's goods at the expense of the local competitors in the area of competition, while its sales and returns from the remainder of its territory remain unchanged. The local competitors may either maintain their sales by cutting their prices and thus reducing or eliminating profits, or they may maintain their prices and lose sales to the large manufacturer. Whichever course they choose, the result affects their entire business. In the meantime, the large manufacturer may have lost some revenue in the area of competition, but this effect is minor because the great majority of its sales are made outside the area of competition. The obvious result is potential disaster for the local sellers.

The problem of fashioning a suitable order arises when the Commission proceeding has determined the existence of a primary line discrimination with the requisite injury to competition or tendency

8. *Matter of Samuel H. Moss, Inc.*, 36 F. T. C. 640 (1943), affirmed *sub nom. Samuel H. Morse, Inc.* v. *Federal Trade Commission*, 148 F. 2d 378 (C. A. 2, 1945).

to monopoly and outside the protection of the provisos to Section 2(a) of the Clayton Act. The Commission's task is to fashion an order that will terminate this method of competition without imposing an inflexible price structure on the market.

One type of order prohibits selling to any purchaser at prices lower than those granted to any other purchasers where the respondent is in competition with any other seller. Another type prohibits selling to any purchaser at a price which is lower than the price charged any other purchaser engaged in the same line of commerce, where such lower price undercuts the price at which the purchaser charged the lower price may purchase products of like grade and quality. The latter type of order was first used in the *Maryland Baking Company*[9] case, which involved a typical area price discrimination. Although the Commission has used this same form of order in some subsequent primary line cases, I must confess that I do not believe it solves all the problems and I am not completely happy about it.

Both of the types of orders I have mentioned are aimed at primary line discriminations that *undercut* the local competition. In each case, there is a degree of built-in flexibility in that the respondent may always react immediately to the downward price moves of his competitors. Perhaps this only makes clear the protection that is afforded by the "good-faith-meeting" proviso. But a different problem is presented in the event the local competitors should raise their prices *above* those of the respondent. According to the terms of those orders, the respondent would be required either to sell at a uniform price everywhere, or at a higher price in the area of local competition than elsewhere, or at a price not lower than that of his local competitors. Thus, such an order would seem to place in the hands of the local competitors, under certain circumstances, the power to dictate respondent's minimum price in a rising market.

Still another type of primary-line order, tailored for a special situation, is one that prevents respondent from reducing prices in any market in which it is in competition with any other seller unless it proportionally reduces prices everywhere. This order is aimed at preventing local price cuts even though they may not undercut the prices at which the local competitors are selling. Although it might seem at first glance to impose an inflexible national pricing system upon the respondent, the *Ruberoid* doctrine prevents this. This is so because, in any new factual situation, the respondent could avail itself of the "good-faith-meeting" proviso or the "cost justification" proviso. Therefore, the order would merely prevent the kind of local price discrimination that had already been litigated and found to be illegal.

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9. *Matter of Maryland Baking Co.*, F. T. C. Docket 6327 (June 29, 1956), affirmed *sub nom. Maryland Baking Co.* v. *Federal Trade Commission*, 243 F. 2d 716 (C. A. 4, 1957).

I am sure that you will appreciate from the examples I have given that drafting orders in price discrimination cases is not an easy job.

In concluding my remarks, let me repeat again that it is always the aim of the Federal Trade Commission to fashion an order that will effectively stamp out the illegal practice and, at the same time, be fair to all parties concerned. I am frank to admit that we have not always been satisfied with the results of our efforts.

The Commission does not adopt the intransigent attitude of Lewis Carroll's Humpty Dumpty that "when I use a word . . . it means just what I choose it to mean—neither more or less." Rather, the Commission is willing to be shown its errors and is anxious to draft orders that all may understand and obey.

Let me emphasize, however, that you lawyers who represent the business community also have an obligation. Congress laid down the Robinson-Patman Act a long time ago. You will agree that there is no indication that it will be repealed. It is here to stay.

Carping and destructive criticism will be of no avail to your clients. It is your duty as lawyers, just as it is our duty as administrators, to see that the business community bides by the Robinson-Patman Act. We need your help, including your thoughtful suggestions on the drafting of fair and effective orders, to accomplish this. To the extent you and your clients cooperate, voluntary compliance will replace costly and troublesome litigation. Everyone concerned will benefit from that.