



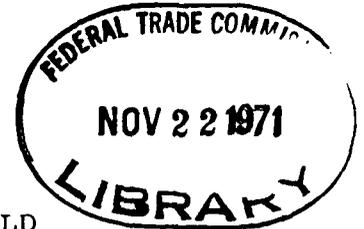
FEDERAL

TRADE

COMMISSION

WASHINGTON, D. C. 20580

For release upon delivery 8:00 p.m., EST,
Thursday, November 18, 1971



THE FEDERAL TRADE COMMISSION -- TODAY'S WORLD

A Lecture By

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in the

ARDEN L. ALLYN AND DEPARTMENT OF ACCOUNTING
LECTURE SERIES

COLLEGE OF BUSINESS ADMINISTRATION
KENT STATE UNIVERSITY
KENT, OHIO

Thursday, November 18, 1971
Auditorium, University School
Summit St. & Morris Rd.
Kent, Ohio

THE FTC -- TODAY'S WORLD

Good evening. I am deeply honored to have been asked to address you as part of the Allyn Lecture Series here at Kent State. The subject to which I shall address myself tonight will, I suspect, inspire in all of us mixed emotions.

Many of you I am sure are already torn between what you feel are conflicting loyalties: one is an allegiance toward the businesses in which most of you are making your careers or intend to after graduation; the other is a sympathy toward the inescapable intellectual atmosphere on college campuses today which decries real or imagined corporate abuses in modern American society.

The tension between these seemingly opposite and irreconcilable attitudes can only be heightened by my presence. As one of the Commissioners of a federal agency created for the purpose of exercising restraints on business, I could easily appear as a threat to whatever intellectual tranquility you may yet possess.

I hope you will be heartened by a sneak preview of the message I intend to deliver. It is simply that the goals of the Federal Trade Commission, and other governmental regulatory agencies, are essentially those same goals toward which business strives. Mutual understanding between the government and private business could be far more easily achieved if each were to examine the other without the fear and hostility often found today.

I.

All of us are familiar with the basic economic model of a competitive marketplace. Businesses design and produce those items which they hope will appeal to consumers. Consumers in turn reward the businessman whose product or service best suits their physical, psychological and sociological needs or wants by buying that product or service.

The reward is the payment of a price which not only covers the costs of land, labor and capital machinery expended by the businessman, but includes a profit for the businessman. He in turn uses this profit to satisfy his wants and needs.

Of course this description is simplistic, but it does point out some of the major values underlying our economic system. For one, we believe that most economic decisions are made by the individuals directly affected; that is, a successful seller must know what products are most desired by consumers. In a similar manner, each individual consumer makes his private decision as to what he will buy, and the assumption is that no one knows better than the individual himself what will best satisfy him.

A second norm, a "quasi-moral" one if you will, is that citizens should be given an equal opportunity to participate in the economic process just reviewed. Artificial barriers based on sex, religion, color and the like have no rational bearing either on what goods or services an individual should be allowed to produce or on which of those items already offered in the market he should be able to purchase.

Finally, the widest possible dissemination of information is necessary for our competitive economy to work efficiently. The phrase "consumer sovereignty" is an apt one to describe this part of our economic philosophy. We want consumers to be aware of all the options available to him when he decides to buy. Without the necessary information, the consumer loses because he may spend his limited financial reserves on one set of goods and services when he would have obtained more satisfaction from another set had he known it was available.

The principle of consumer sovereignty has an important impact on the businessman too. If the consumer is misled by the claims of a competing producer, or if he for some reason is unaware of the existence of our businessman's product, the businessman unfairly loses sales, and thus profits, which rightfully belong to him.

It is safe to assume that most businesses in our country would readily subscribe to the values of private decision making, free opportunity to compete, and the availability of adequate information. None of them are foreign to the American system, and none impose any foreign ideology with which some mistakenly identify any governmental activity in the sphere of the economy.

As a matter of fact, it is precisely those values that have led to governmental participation in economic life. It is not in order to prevent or replace private decision making, to eliminate the opportunity for members of society to participate, or to stifle the free flow of ideas and information in the marketplace, that the Federal Trade Commission was created. Its purpose is the opposite. The Commission has no conceivable reason for existence other than the protection of the fundamental values of a free competitive economy.

II.

The origins of the FTC are to be found in the antitrust laws enacted in the closing decades of the last century. In the closing stage of the period which brought industrialization to this country, public opinion would no longer stand for the abuses of the larger combines which seemed to threaten complete domination of the American economy.

Basically, Americans felt that it was no longer possible for the individual to participate in a meaningful way in the economic process. The individual entrepreneur survived only at the suffrance of a competitor who had the power to manipulate consumer choices in whatever way suited his interests.

Among the tactics used was what lawyers call predatory pricing; that is, reducing the retail price of a product below cost in order to drive competing businesses to extinction. A large firm could afford to sell below cost by subsidizing the effort which profits earned in another area, where there was no competition. Soon there would be two areas in which the large firm had no rivals. Less subtle forms of subduing competition, including that of physical intimidation were also employed.

The response to this situation was the Sherman Act of 1890. It sought, and still seeks, to improve matters by outlawing "conspiracies in restraint of trade". It also declared illegal "monopolization" and "attempts to monopolize" trade in a geographic or product area.

Unfortunately, the Sherman Act turned out to be too vague to be completely effective. In a series of early decisions, the courts found it difficult to determine the exact meaning of the statute, and the end result seemed to be frustration of the competitive ideal rather than its enhancement.

Shortly before the first World War, the experience of the Sherman Act seemed to demonstrate quite clearly that a novel approach to the protection of competition was needed. The second solution was not a substitution of more specific language for the general phrases of the Sherman Act, however.

It was decided that a new enforcing body, an administrative agency, could make up for the deficiencies with which the courts had struggled for 24 years.

The idea of a trade commission had been part of the platforms of each of the three political parties in the presidential campaign of 1912. Giving primary responsibility to such a body was seen as a method that would, as the Republicans put it, "promote promptness in the administration

of the law and avoid technicalities incidental to court procedure." 1/ The technicalities, of course, were the often conflicting and overly restrictive interpretations which courts were prone to reading into the Sherman Act.

At first the new agency was seen as an advisory committee, collecting information on business practices for use by the Justice Department in prosecutions under antitrust legislation. It would also advise businessmen as to the legality of any course of action they might want to follow.

The Federal Trade Commission Act as finally passed, however, created an agency that could not only interpret the law, but enforce it as well. The enforcement technique was, and still is, the cease-and-desist order, which orders a business to end any violations found to exist. It often includes provisions designed to prevent a recurrence of the offending conduct as well.

The standard by which the Commission was to operate was that of ending "unfair methods of competition". This sounds suspiciously like the rather elusive provisions of the Sherman Act which created the difficulties the Commission was to straighten out. Besides being a formulation agreeable to

1/ Republican Campaign Text Book 1912, p. 273

both Houses of Congress, that phrase was considered appropriate because the Commission was provided with an information gathering function. By judicious use of the knowledge acquired, the FTC was expected to develop an expertise in the field of trade regulation which would enable it to give real content to the vague formula of "unfair methods of competition".

It is important to understand the economic philosophy that led to its enactment. This was not an arbitrary intrusion of government into a sphere in which it did not belong; rather it was the expression of a need felt by the consumer and the businessman alike, a need for an institution designed to protect the values of a competitive economy.

One of those values was that of assuring each individual that he would retain the right to enter the market as a producer of goods or services, free of the arbitrary whims of others who might want to restrict such entry. It was not the intent of this legislation to substitute governmental decree for private decision making, and indeed it would be impossible to support any contention that the Federal Trade Commission has ever instructed the business community that certain goods were to be produced or that others were not to be produced.

By the mid-1920's, Gerard Henderson in his book, The Federal Trade Commission, noted with a hint of awe that the Commission was working "with a personnel of more than 300 men and women and an annual appropriation of nearly a million dollars". 2/ While such a commitment of resources astounds no one in these days of multi-million dollar defense budgets, it was at least an indication that the American people of the era between the World Wars were serious in their intent to see the Commission firmly established as an economic institution.

Unfortunately, the commitment was not strong enough to enable the young agency to do much more than conduct studies. Its docket quickly became hopelessly overloaded, and court decisions viewed Commission activity on the monopoly front with more than a little hostility.

Increasingly the FTC shifted emphasis from control of trusts to less urgent unfair practices, and finally settled down to a more passive role of providing economic studies requested by Congress. These studies proved to be more useful than might have been anticipated: one led to the Public Utility Act of 1935, and another recommended the creation of a regulatory body which eventually became the Securities Exchange Commission.

2/ G. C. Henderson, The Federal Trade Commission, xi (New Haven, 1925).

Surprisingly enough, the almost cataclysmic period of change which enveloped the American economy in the Depression and New Deal eras did not immediately revive the FTC. Poor economic conditions decreased the amount of business activity in general and made an attempt to restrict the activities of those firms which did manage to remain solvent seem a rather poor idea.

In addition, the National Industrial Recovery Act, one of the most important of the New Deal legislative innovations, did not stop at allowing inter-corporate communication and collusive activity. Under the "Codes" authorized by that Act, businesses in many segments of the economy were compelled by law to make and honor agreements which restricted competitive activity. There seemed little room for an antitrust agency in that scheme.

The NIRA was in effect for a relatively short time before it was declared unconstitutional by the Supreme Court, and the FTC and antitrust began to assume a new respectability.

1938 proved to be an important year in the Commission's history, and it might well be considered the starting point for those activities which make the FTC relevant to the economic world of the 1970's. In that year the Wheeler-Lea Act amended the Commission's jurisdiction to include coverage of "unfair or deceptive acts or practices". Translated from the legalese, the phrase gave the FTC the power to issue cease-and-desist orders in matters of false advertising, and ranked the consumer along with the business competitor as worthy of the Commission's attention.

III.

At present the FTC administers 12 separate statutes, 9 of which are primarily for the benefit of the consuming public. Some provide minimum standards for products placed on the market. The Flammable Fabrics Act, for example, directs the Commission to prevent the sale of any interior furnishings or clothing which do not meet the flammability standards set by the Department of Commerce.

Most of these Acts, however, cast the Commission's work in the more traditional role of preserving a truly competitive economy. The Textile Fiber Products Identification Act and the Wool Products Labeling Act, for example, authorize the Commission to assure that clothing labels plainly disclose

the materials which have been used in manufacturing garments. This neither prevents the manufacture of any product nor instructs the consumer as to what he should and should not buy. It merely assures that the consumer will have as much relevant information as possible before he makes his purchasing decisions. In addition it protects the businessman by assuring that his business will not be taken by a competitor who misleads the consumer into making a choice he would not otherwise have made.

While the FTC has had jurisdiction over interstate matters of consumer protection, I must admit that it has not always acted as wisely as it might. One attempt to aid the consumer led to a 1943 consent order which prevented a television repair school from representing that there was a great future in the field. This type of case has led to two very serious criticisms of the Commission's consumer protection work.

The first of those criticisms is that the FTC buries itself in trivia for the most part. Since most of our work is done on a case-by-case approach, certain types of petty fraud can end up consuming enormous quantities of the FTC's time and staff work, with only marginal benefits to the consumer or anyone else. One might point, for example, to a certain segment of the chinchilla raising industry. There have been countless cases of small fly-by-night operations which lure the uneducated with promises of enormous riches. Once the hapless consumer has spent \$500 to \$1000 for his stock, he finds that the animals do not breed quickly and easily, and the pelts do not bring fabulous sums on the market.

Certainly no responsible businessman would claim that the government is intruding beyond its proper role in the economy if the FTC forbids these firms from telling their victims that the purchase of a small rodent is the equivalent of a train ticket to El Dorado, the fabled city of gold. But, typically, the businesses which operate in this manner come and go quickly, and it is not surprising to find that such an unscrupulous operator has gone out of business by

the time a cease-and-desist order is issued against him. Since the Commission is not empowered to award damages to those already defrauded, the cease-and-desist order in such a case is relatively meaningless as far as its impact on the economy is concerned.

An alternative to the case-by-case approach is found in the use of Industry Guides and Trade Regulation Rules. To generalize very broadly, these are specific rules of conduct formulated for various industries. They are issued after careful economic study, the solicitation of comments from the affected industry and the public, and in the case of Trade Regulation Rules public hearings as well.

Unfortunately, the Commission's use of these devices subjects it to the second set of criticisms. It is claimed, for instance, that issuing "do's and don't's" for an industry condemns all the businessmen in that industry, whether or not they have committed any unfair or deceptive acts.

It is also said that this constitutes an unwarranted restriction on the economic freedom of many businesses based on allegations of unethical conduct which may or may not actually have been indulged in by their competitors.

However, under any logical standard, neither criticism justifies the conclusion that FTC practice in this area represents an encroachment by government on the free enterprise economic system.

Indeed, the cease-and-desist order in an individual case normally calls for far more complete information to be given when a product is offered for sale. In this way, it reinforces the values of a competitive economy.

Similarly, Guides and Trade Regulation Rules typically require that certain claims can be made only when specified additional disclosures are provided, or even simply that no claims be made unless they are actually true.

A sample of the latter type of rule is the recently adopted rule covering the Advertisement of Special Offers in Supermarkets. It binds a store only to having a reasonable supply on hand for sale to consumers when an item is advertised as being on sale at special prices. A store is free to impose any conditions on the purchase, and even to limit the amount or number of special items to be sold, as long as that information is clearly provided.

IV.

When the Commission's role was expanded to include consumer protection, the antitrust function was by no means forgotten. The Sherman Act is still enforced with vigor. Modern business conditions, however, have led to the passage of other antitrust legislation.

Of particular importance is the Clayton Act, Section 7 of which prohibits a corporation from acquiring the stock or assets of another enterprise if the result is "substantially to lessen competition" in a particular line of commerce in any section of the country.

Being businessmen and future businessmen, you do not need to be reminded that acquisition is a basic way of life in today's industry.

Your first impression may be that the Clayton Act excuses the government from its role as a neutral referee in business affairs and authorizes it instead to appropriate the power to make decisions which rightfully belong to the private sector. A closer examination reveals that the purpose behind Section 7 is to assure that business does not become dominated by large and powerful corporations which can by sheer size intimidate others and discourage attempts by others to enter the market.

The Department of Justice, which administers the anti-trust laws jointly with the FTC, has established guidelines for governmental interpretation of the phrase "substantially to lessen competition". Attention is focused on market structure, for the most part, because the behavior of firms in an industry is often governed by the structural characteristics of that market.

The term market structure is simply a convenient way of referring to each industry characteristics as: the numbers of buyers and sellers in the market, the market shares of each, and the presence or absence of economies of scale. When market structures are examined, industries showing a trend toward concentration are watched particularly closely.

A merger may be challenged for reasons not based on market share figures. A merger of a "substantial firm" and a very small one is considered suspect if the smaller firm has some assets which might give the larger firm an "unusual competitive advantage".

Vertical acquisitions, those in which a supplier buys a customer or vice versa, are considered anti-competitive if they raise the cost to others of entering either market, or if they disadvantage existing non-integrated firms in ways unrelated to economic efficiency.

The most popular form of combination in recent years, of course, has been the conglomerate merger. It is as difficult to frame guidelines for the conglomerate merger as it is to define exactly what the term means, but some guidelines have been framed in this area as well.

These are not arbitrary regulations designed to harass the honest businessman. Indeed, they do not present detailed instructions as to how businessmen may and may not act. They are intended merely as reference points, and properly used they provide the corporate planner with an indication of how federal agencies and courts may view a proposed transaction.

The guidelines are available to the public, and the staffs of both agencies regularly provide advice in borderline situations or for those with other special problems. If the businessman is willing to use the information available to him in planning a corporate combination, it is unlikely that he will find the United States unexpectedly peering over his shoulder.

V.

Clearly none of the current activity of the FTC interferes with the three basic values of the free enterprise system which I outlined earlier. Private decision making, on the part of producers as well as consumers, is encouraged--as long as one does not attempt to induce others to believe that a proposition is true when it is not. Certainly the

goal of providing a maximum of information on which economic decisions can be based is enhanced. And, finally, the Commission's antitrust policies provide everyone a fair chance to participate in the economic system, without the fear that overly powerful elements might arbitrarily diminish his chances of competing successfully.

VI.

So far we've seen the past and present operations of the Federal Trade Commission, and there appears to be nothing to indicate a disregard for the ideal of a freely competitive economic system. But the more important issue is the outlook for the future. Is there a real threat that government is about to replace private enterprise, that all business decisions will soon be made by an indifferent bureaucracy that will pay no heed to our economic heritage? I can foresee no such radical change, at least during the period in which you will be carving out careers in modern business.

It would be more than a little naive to say that government participation in the economy will not continue to grow; we all know that it will. But our country is continually changing and growing, and business is exploring

areas undreamed of two decades ago. Phenominal growth in such industries as plastics, computers and franchised foodstores have created a new economic environment. The corporate conglomerate has developed from an occasional oddity to a standard form of business organization. Only the most unrealistic of people could expect government to contain itself in size and function to the standards of the late 1940's or 1950's.

The real question is: What form will expanded government economic activity take? The answer lies, I feel, in the attitudes which you and those who follow you will bring to corporate enterprise as the executives of my generation are gradually replaced by the students now at Kent State and other fine schools.

No one can ignore the current trend known as the "consumer movement" and the increased activity it has brought to the FTC and other governmental agencies. Consumers will increasingly demand more product information, better quality control, more extensive (and more scrupulously honored) guarantees.

The factors that have led to the current dissatisfaction with our economy are not difficult to trace. The individual consumer is faced with a bewildering array of technically and mechanically sophisticated products, all of them promising unprecedented ease and convenience for those who buy. It is useless to explain that consumers misinterpret the claims businessmen make for their products, or that they simply expect too much of the items they buy. The truth is that it would be impossible for the average individual to become sufficiently well-acquainted with the mechanical and engineering designs of the cars, televisions, and even the electric toothbrushes that are offered on today's market.

The burden has shifted to the businessman to provide all the relevant information about his product. The demands being made by consumers simply represent the changes which must be made in the system in order to preserve the philosophies and values underlying free competition.

Government agencies in general, and the Federal Trade Commission in particular, are not anxious to tell the businessman what to say or to set standards and specifications for consumer products. But if the need becomes urgent enough, the government will be called upon to exercise its influence in areas it would rather leave to others. That call, if and when it comes, will be impossible to ignore. It has done so, for example, in the field of automotive safety.

It was gratifying to see, when the FTC recently initiated its pilot advertising substantiation program, that the automobile manufacturers cooperated so well. As long as the information which consumers need so desperately is not withheld, it is unlikely that the FTC will feel it necessary to tell manufacturers what claims they may and may not make, or to require prior approval of any claims intended for use in advertising.

Similarly, enforcement of the antitrust statutes can no longer be regarded as an unwarranted complication of the businessman's affairs. The goals sought by the legislation are those closest to the heart of the American ideal--free competition and reasonable opportunity to gain access to markets. The modern corporation must learn to welcome this sort of government participation, and I feel that enlightened leaders such as yourselves can inject just such an attitude into the modern corporation.

On the basis of my experience at the Federal Trade Commission, I think I am fairly safe in predicting that government and business need not become adversaries in the future. The role of the Federal Trade Commission will most likely remain that of an advisor and a partner with business in the effort to maintain and strengthen the competitive ideals of private decision making, the free flow of information, and freedom of entry into the marketplace.

The Commission is eager to assist, not to overpower, business. The choice belongs to the nation's businessmen and the students of business on college campuses throughout the United States. If you bring to the modern corporation an understanding of the problems of the consumer, and a willingness to respond to the consumer demands generated by the modern industrial market, there is no need to fear the power of government. Our preferred role is cooperation, not domination. If you, too, are willing to cooperate, the free enterprise system will continue to thrive in modern America.